FINANCIAL HISTORY
OF CANADIAN GOVERNMENTS

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FINANCIAL HISTORY OF CANADIAN GOVERNMENTS

A STUDY PREPARED FOR THE

ROYAL COMMISSION ON DOMINION-PROVINCIAL RELATIONS

BY

STEWART BATES

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Financial History of Canadian Governments

EDITORIAL FOREWORD

Stewart Bates, then Secretary of the Economic Council of Nova Scotia, and now Professor of Commerce at the University of Dalhousie, was retained by the Royal Commission on Dominion-Provincial Relations to make a study of the financial history of Canadian governments. Professor Bates was asked to include a review of the public finance history of the Dominion and of each provincial government with particular emphasis on the relation between fiscal policy, economic policies, and underlying economic developments. It was expected that his analysis of revenue powers, governmental functions, and debt growth would indicate the points in the Canadian public finance system at which important strains have developed.

A large part of Professor Bates' material was supplied by the returns to the financial questionnaire circulated by the Commission's Public Accounts Inquiry under Mr. J. C. Thompson, and by the regional and general economic studies made under the direction of Dr. W. A. Mackintosh, although it was not possible to complete these studies in time to permit their fullest utilization. The method of presentation and any expressions of opinion are solely the responsibility of the author, and not of the Commission.

Professor Bates finds a clear cut objective in the fiscal policy of both Dominion and provincial governments prior to the War. This was the development of the country's resources by extension of its frontiers and assistance to private enterprise. Freedom from other burdens and responsibilities, partly as a result of the orthodox laissez-faire policy of governments in other activities, and partly as a result of the young structure of the country and of the general prosperity accompanying the 1896 to 1913 expansion, put the

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governments in a financial position to pursue this policy aggressively. Although this fiscal policy was related to such national economic policies as western settlement, railway construction, and tariff, Professor Bates finds a notable lack of co-ordination between the governments concerned, and points out that the combined actions of ten independently operating governments was not likely to be a well integrated programme, or the most appropriate one for the economy. Over expansion was likely, and occurred in some fields, and neglect in others. The rapid expansion of the period, however, obscured the bad effects of non-coordination of capital programmes, tax systems, and current expenditures.

The War saddled the Dominion with a heavy debt and heavy railway obligations, and by marking the end to further frontier expansion (with a few exceptions), ushered in a period of economic readjustment and social philosophy change which had important implications for fiscal policy. Provincial governments were not initially as hampered by debt in the post-war period, and were to some extent able to step into the gap left by the Dominion and pursue intensive developmental policies. In the thirties, however, the cumulative effect on their debts of their taxation policies and capital programmes in the twenties, and of their depression burdens, handicapped positive policies.

Throughout the post-war period, when adjustment had to be made to basically changing economic conditions and trends, and when the proportion of the national income which passed through governments' hands mounted to unprecedented levels, the need for a coherent fiscal policy increased greatly. Co-ordination of government investments, taxes, and expenditures, and integration with tariff, transport, monetary and other economic policies were necessary to minimize the cost of government on industry and to maximize its efficiency. The new importance of public finance operations and fiscal policy was

not recognized; even in recent years, when one-third of the national income is directly redistributed by governments fiscal policy has been considered as something determined by prevailing economic conditions rather than as a governing factor in itself.

As a result of this traditional attitude, of the accumulated debt burdening all layers of government and of the economic outlook, Canadian governments are now faced with two major problems. One is the dilemma which must be faced in the next depression. Then, (particularly in view of the present inability of governments to balance budgets even in "normal recovery" years) reliance on a negative policy as in the last depression will probably result in deficits, cuts in expenditure, increases in taxation, further unemployment, larger deficits, and increasing debt. On the other hand, an attempt at a positive policy of increasing expenditures and reducing taxation will also increase debt. As in the past, but on an ever increasing scale, lack of co-ordination between governments' fiscal policies will aggravate the cyclical swings, and prevent any constructive use of the powerful weapon of public finance action.

This leads to consideration of the second major problem peculiar to federal organization, which is whether a compromise can be found to preserve local autonomy and provincial rights without completely hamstringing effective fiscal action and involving costs and waste which the Canadian economy can no longer afford. There are many related problems, made more complex by the federal structure, such as the policy which should be adopted for the chronically 'needy' regions. Of basic importance, Professor Bates suggests, is the economic outlook, and the need for policies appropriate to the altered economic circumstances, and to the political and social structure which exist in Canada today. Throughout

he emphasizes the need for an integrated fiscal system and coherent policy for effective action, and the disabilities which will result if it is lacking.

Following a brief introduction which discusses some general considerations of Canadian public finance development, Professor Bates reviews seriatim the financial history of the Dominion and provincial governments.

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Introductory Summary

At the beginning of this study on the fiscal policy and financial position of Canadian governments it might be helpful to single out some of the factors that have dominated the history of Canadian public finance, and to note their relevance to present-day budgetary problems.

1. Character of Canada's Financial History

Contrast between pre-war and post-war fiscal policy in Canada

The Great War stands out as the major turning-point in Canada's financial history. Before that time the fiscal policy of the Dominion government, as disclosed by the nature and extent of its expenditures and tax methods, was directed in a positive way at one central purpose, namely,the extensive expansion of the Canadian economy. Since the War, however, for reasons to be given later, the Dominion government has taken a more negative attitude towards fiscal policy: fiscal action came to be something dictated to the Dominion by the economic and financial characteristics of the post-war period. The provincial governments, from the War to 1930, tended to follow up the pre-war Dominion policy of using public finance as an active means of economic expansion, but they too, after 1930, have considered it expedient to take a passive attitude towards public finance. In short, it might be said that Canadian governments as a whole were traditionally committed to the active pursuit of economic development through public finance, but that since the War, and especially since 1930, they have passively accepted the public finance position as it has been determined for them by the economic exigencies of the time.

It is necessary to expand this summary statement, and to examine its implications.

Nature of pre-war fiscal relations between Dominion and provincial governments.

From Confederation up to the Great War the dominant purpose of Dominion fiscal policy was to develop the resources of the country by extension of the "frontiers" and by assistance to private enterprise. This end was pursued more vigorously at some times than at others as succeeding parties in power found expedient opportunities and means, but the aim remained fairly constant. The policy took the form of pushing settlement, supplying an all-Canadian transportation system, and encouraging home production by tariffs and other means.(1) In Canada, as elsewhere, the pre-war concept of good government was the minimum of government, but in Canada the minimum was a very different thing from that in older countries. From Confederation Canada's "minimum" included positive governmental action to stimulate settlement and private enterprise.

But while the Dominion government, in its relations with private enterprise, thus generally adopted a positive attitude towards development, it did not, in its relations with the provincial governments, adhere so positively to the same principle. The provinces were not then regarded as agents directly concerned with the stimulating of economic development.

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(1) The methods by which Canadian governments (Dominion and provincial) have encouraged private enterprise at one time or another are many. Some may be enumerated: (a) Direct subsidies to industries, (b) Tariffs, (c) Building of railways and subsidies to transport, (d) Alienation of natural resources, (e) Monopoly licences, or special privileges, (f) Direct loans or cheap credit, (g) Relief of some enterprises from special imposts laid on others that compete with them, (h) Collateral aid to certain industries; e. g. to the coal, steel and railway equipment industries by railway construction; to the automobile industry by road building; to the construction industry by housing loans, (i) Government orders.

The extent to which many private enterprises have always been dependent on government intervention has not been inconsiderable in Canada.

Before the War discussions of Dominion-provincial relations were concerned more with the size of the Dominion subsidy to the provinces than with their mutual concern over economic development. The subsidy question was not, of course, unconnected with the question of economic expansion, because, as the provinces undertook greater responsibilities and served growing populations, they required larger revenues. But the statutory subsidy from the Dominion government was not flexible, and as provincial expenditures increased, the subsidy became a constantly diminishing proportion of the provincial revenue requirements. In 1870 the subsidy had provided 60% of the total provincial revenues: by 1890 the proportion had fallen to about 35%: by 1920 it was less than 15%, and by 1930 less than 10%. Faced with an almost static grant from the Dominion government, and with expanding expenditure needs, the provinces sought, sometimes singly and sometimes collectively, readjustments of the subsidy arrangements. And the Dominion government did make revisions of the subsidy at various times, sometimes to single provinces and sometimes to the provinces as a whole. In this indirect way, the Dominion still adhered to its policy of national economic development, for the subsidy revisions were made to remove political disputes that might, among other things, have impaired economic progress, and they were also made to counteract what seemed to be a comparative weakness in the financial status of some province. But, it is important to note, the statutory subsidies to the provinces have not increased significantly since Confederation. The Dominion's realization that financial concessions to the provinces might be made at too great a price, and that they could be made only when the Dominion had ample revenues of its own, reduced the potential variability of the statutory subsidies. Indeed it was not until 1930 that Dominion grants to the provinces began to rise with any significance, firstly in the expansion of conditional grants, like those for

old age pensions, and secondly, in the increased assistance to the provinces to meet the special problem of relief in the depression years. These latter relief grants alone have exceeded any previous inter-governmental transfers in Canada. Accordingly, while Dominion-provincial discussions on the subsidy question have been relatively important in Canada's political history since 1867, the actual amounts of revenue involved did not change significantly in Canada's financial history until after 1930.

Lack of co-ordination of fiscal actions in Canada before the War

While the pre-war discussions on Dominion-provincial relations emphasized the subsidy question, a more fundamental relationship between the governments was implicit, because both the Dominion and the provincial governments were directly interested in the problem of economic expansion. The provinces, as well as the Dominion, were involved in aids to railways. And the provinces' concern with economic development required them to make expenditures on colonization, to provide the equipment of settlement (government, justice, roads, schools, hospitals), and to stimulate the utilization of their provincial resources by other methods. These expenditures of the provinces (including their municipalities) rose very rapidly in the pre-war boom period (1896-1912). But since there was no conscious or explicit recognition of their mutual concern in the matter of economic progress, the Dominion and the several provinces, each within its own sphere, pursued their own particular developmental policy without much reference to the policies being followed by other Canadian governments.

There was danger, which now seems obvious, in this lack of co-ordination. The danger arose not only from the fact that the Dominion and the provincial governments divided jurisdiction on certain matters (e.g. agriculture, etc.), and that therefore some areas in the field of their mutual concern

might receive overlapping attentions while other areas suffered some neglect. That danger has always been present under divided rule, but it was dwarfed by the more important economic problem of federalism in a growing country - the fact that the combined result of the economic aims of ten independently operating governments might not be the one at which a well-integrated national economic programme would aim. There was the danger that each government, especially when it subscribed to the Gladstonian lesson that the budget was a means of civilization and progress, would regard these ends from a local, and not from a national, standpoint, that it would extend its institutional equipment (schools, hospitals, public buildings, works, etc.) according to its own hopes concerning the future of its territories, that it would engage in capital works, government enterprises, and aids to local industries in order to hasten its economic expansion or to try to keep up with the pace of expansion being established in other regions of the country. In short, the lack of co-ordination in fiscal policies and their pre-occupation with local rather than national economic development, were likely to exert varying pressures on the distribution of settlement and industries throughout the country. Sometimes these pressures exerted by fiscal actions would reinforce the pressures being exerted by natural factors, like the distribution of natural resources, and would thereby intensify the "pull" of that locality on certain industries, and sometimes these local fiscal pressures would strengthen the power being exerted by national policies, like the tariff, and would thereby help to speed up development in the particular area. But occasionally local fiscal encouragement applied a pressure opposite to those being exerted by natural forces and by Dominion national policies, and thereby helped to maintain or even encourage local industries which would otherwise have proved to be uneconomic. Since provinces could not encourage local economic expansion by erecting tariffs around

their local economies, they were likely to try to reach the same end by more direct forms of industrial encouragement, and this, in turn, was likely to reflect itself later in their debt structures. And since their fiscal actions were not integrated, there might result over-expansion of certain equipment, e.g. in railways. And since fiscal actions were aimed at securing the maximum local expansion, there was little chance that the ultimate distribution of industries and settlement would be the most economic from the national standpoint. Indeed the fiscal actions of the several governments were more likely to further the economic regionalism which nature seems to have decreed for Canada when selecting her geography.

But these dangers do not seem to have been considered in the pre-war period. Questions of racial and regional particularism had, it must be recalled, come to the surface during the depression in the 80's and early 90's, but the emergence of the world trade boom after 1896 communicated so great an economic stimulus to Canada that these questions rapidly gave place to the new confidence that the 20th Century belonged to Canada. And during the boom (1896-1913), the Canadian economy was expanding so rapidly that in financial matters the projects of most of the governments seemed quickly to justify themselves, and the need for securing efficient co-ordination of the capital works of the different governments, and of their tax systems and current expenditures, was never very obvious. In the post-war period, however, when new frontier expansion was confined to only a few wheat and mining territories, and when Canada's economic vulnerability in depending on a limited number of great exports became increasingly evident, it became also apparent that the pre-war unco-ordinated economic policy had in itself resulted in two significant difficulties. On the one side, the volume of transport equipment that had been provided in the pre-war boom became in itself a problem. On the other, the great extension of frontiers that

had been made, and that enclosed the areas specialized to yield the great exports, were economically sensitive to the vagaries of international trade which in itself began to exhibit new instabilities. A question now began to arise: whether the extensive development of the country had been pushed to the neglect of intensive development, whether the economic actions of the independently operating governments had been directed too much at frontier expansion, and too little towards making the best use of already developed resources, too little towards the encouragement of industrial innovations and adaptations, towards the search for new commodities or new products that might be derived from the natural resources, towards the stimulation of new or more efficient processes of production.

New significance of uniform, fiscal policy for post-war problems

The post-war economic conditions called for government economic policies at least as positive as those of the pre-war period. But further frontier-expansion (and the provision of the equipment of settlement and communication by governments) could no longer be looked to as solvent to all economic difficulties. The rate of economic progress was slowing down, although the consequent changes in the structure of the Canadian economy were difficult to disentangle from the short-period disturbances that arose out of the post-war international trade position. Ideally what was wanted was a national policy which would overcome, or at least mitigate, the observed weaknesses of the Canadian economy; and which, to that end, would use in a co-ordinated way all the financial powers and instruments of the various governments. But in fact no such integrated national economic policy was forthcoming.

The difficulty of formulating an appropriate policy arose, first, out of the complex nature of the economic problems that confronted the country and the consequent lack of precise ideas about the objective and the technique of attaining it;

and secondly, because of debts, on a scale unknown and unimagined before 1914, which have hampered Dominion action ever since the War, and provincial action especially since 1930. Some attention should be given to each of these difficulties that confronted Canadian governments as a whole.

Dominion fiscal action since the War

So far as the Dominion government was concerned, both difficulties were present. At the conclusion of the War, its debt had risen from $521 million in 1913 to $3,520 million in 1921, the War and the railways having been the main contributors to the change. As a result, its current budget had a large uncontrollable sector of expenditures after the War. Net debt charges, pensions, and transport subsidies had formed 38% of the pre-war budget, but after the War the proportion was nearer 65%, and it increased in the depression after 1929. The new level of the Dominion's commitments, and the large proportion of necessary expenditures in the ordinary budget, reduced the Dominion's desire to make new expenditures: the tendency was rather to await buoyant economic conditions that would increase revenues and help to reduce the debt, as happened in 1926-8. Consequently, the Dominion's concern with national equipment involved mainly the rehabilitation of the railways it had taken over and the rounding out of the pre-war programme - in itself a very substantial undertaking. Contributing also to the unwillingness to indulge in new works was the recognition that the economy probably required little more extensive equipment. That had been the principal means adopted before the War to encourage national and regional development. But after the War, further extensive expansion did not appear to be appropriate; intensive development of industry within Canada seemed more desirable. The post-war economic conditions and the changing nature of international trade called for some readjustment in the Canadian economy, not so much in the direction of further extension of frontiers and exploitation of resources, as in the search for methods of increasing the utilization of already developed resources, the search for methods of deriving new

commodities and new qualities of products, the search for more intensive manufacturing methods to be applied to Canada's raw materials. But this post-war problem called for a clear-cut, coherent national economic policy. And that was difficult to provide because public opinion had no precise views about either the end or the means. Canadian governments had never tried to integrate their investments, their current expenditures and taxes, as a means of reaching a national objective, nor had they ever attempted to relate any such fiscal action to tariff, transport and monetary policies in order to provide a coherent national economic policy. Public opinion interpreted national (economic) policy as tariff policy, while the other elements, and their inter-relations, were not considered. Since public opinion was inert, it is not surprising that the Dominion's economic policy, in face of the new problems, was a negative one in the post-war period. The Dominion felt it necessary to be cautious about adopting even a dynamic fiscal policy because it was already committed to a high level of necessary expenditures. In these conditions, the Dominion tended to wait for a boom in external trade, because that would raise the Canadian national income, would encourage the sort of intensive development that was necessary, would add to the revenues and tend to reduce the debt burden in the Dominion budget. Unfortunately, in the post-war period, the number of booms in international trade has been disappointingly small; and the present position of international trade does little to encourage the belief that the trade position of the next few years will be greatly improved.

Provincial fiscal actions since the War

So far as the provinces were concerned, the developments of the post-war period raised their debts and their current expenditures. On the one side, the change in opinion on social questions, coupled with the change in the rate of economic progress, involved the provincial governments in new welfare expenditures. Even if the economic position remained fairly satisfactory, the gradual social stratification of Canada,and the example of growing social services in other countries,were in themselves likely to lead to new levels of social service in the future. Welfare and similar services are in their

infancy in Canada.But if the economic position were disturbed,the provinces were likely to encounter a sudden increase in their relief and welfare costs. If the depression were a large one, this would affect not only the current expenditures of the provinces, but also their debt structure, as happened from 1929 onwards. The provincial debt picture was coloured also by another circumstance. All the provinces, in greater or less degree, were affected by the change in the long term rate of economic progress in the post-war period. In only a few areas was further frontier expansion possible: in most provinces some need was felt for encouragement to local industry, for further intensive development, and this tended to become a provincial problem. In contrast to the Dominion's negative attitude towards development, the provinces, because of the constitutional distribution of powers, and because of their close contact with local resources and local needs, felt it necessary to expand investments that seemed likely to strengthen their economic position. Between 1920 and 1930 provincial debt was doubled, some 44% of the increase going to highways, 25% to utilities, 12% to public works, about 10% to advances to local industries (from which little interest was received), and the remainder to miscellaneous purposes, including deficits on current account. During this period therefore, the economic aims of the provinces tended to be more positive than those of the Dominion: but there was still little or no co-ordination of effort between the provinces. Indeed there is some evidence of inter-provincial competition for both new and old industries during this period. Attempts were made to expand local road transport, power and other undertakings, (notoriously in the case of pulp mills), without much regard for the effects of these actions on the country's existent equipment in transport, coal and other affected industries. Such inter-provincial competition was not without advantages, but some considerations suggest that these advantages were subject

to qualification. In Canada, with its economic regions and its regional loyalties, the competition of industrial innovations, whether due to public or private investment in some area, do not always drive older and less efficient industries out of business; it often leads to demands for government support of the industries that are adversely affected by the new developments, and thereby induces the government in the affected area to try to maintain its local industry or to call for help from the Dominion government in the form of a direct industrial subsidy, or alteration of the freight charges in the affected commodities, or an increased subsidy to the provincial government so that it may directly support the area affected by the new developments elsewhere. In this way, technical progress in one industry or region does not always represent a net economic gain to the country as a whole. Before the gain can be calculated, it is necessary to ask whether the technical change in some region has provoked new government support of some competitive industry or region, and whether the governmental action is thereby hindering the occupational, industrial or regional readjustments necessitated by the initial technical change. In another way also the inter-provincial competition created some disadvantages. In their labour legislation the provinces revealed some unwillingness to make advanced legislation lest that might penalize the industrial prospects of the province. In the welfare services as a whole, the lack of co-ordination was very marked. There was little recognition that the several provincial policies in matters of public health, welfare and labour legislation were each phases of the general problem of poverty which in turn, depended on national more than on local economic conditions. The form of administration, and the consequent lack of co-ordination were leading to dangerous policies.

Fiscal Actions of all Canadian governments in the depression after 1929

After 1929, the need for industrial encouragement and for a coherent national economic policy was greater than before, especially in those areas dependent mainly on external trade, but most provinces then considered it necessary to raise their taxes, to curtail their capital and even current expenditures, and to devote most of their new borrowings and revenues to direct relief and to certain types of welfare expenditure.

In the depression the Dominion also had to devote large sums to relief financing and to special "depression" expenditures. And so, after 1929, Canadian budgets, which had always to some extent been instruments for stimulating at least local economic development, became largely instruments for transferring income to rentiers (2) and to those requiring relief. On the expenditure side, the great curtailment of new capital works, the failure to maintain existent equipment, the reduction in current expenditures on health, education, public domain and highways, and the increased charges for debt and relief, all reflected the passive role of government expenditures in face of the depression. On the taxation side, the increases in tax rates, almost regardless of the effects of this action on depressed private enterprise, and almost regardless of the equity or justice of the tax system as a whole, also reflected the negative attitude towards economic development. There was little or no co-ordination of Dominion and provincial revenues and expenditures, no general, uniform fiscal policy.

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(2) The attempt of the Dominion government to lower interest rates after 1932 was aimed at reducing the burden of the transfer to rentiers.

Yet since these budgets began to absorb one quarter of the national income (or more than a third if municipal governments are included), they were presumably affecting private enterprise. But there was no conscious fiscal policy that aimed at producing the most desirable (or the least undesirable) group of effects. Fiscal action was still "accidental", not viewed as a whole, nor in relation to monetary, transport, and tariff policies. Indeed in the "timing" of their fiscal actions, the different Canadian governments tended to aggravate rather than smooth the disturbances imposed on the Canadian economy by the movements in external trade. When external trade was prosperous, and the Canadian national income rose, most governments tended to lower tax rates and to increase capital expenditures, thereby giving an extra impetus to the boom that was in progress(1925-8). With the depression and the decline in external trade, the governments increased their taxation, cut capital works, and added to the forces creating depression. Since the fiscal actions of the different governments were not co-ordinated, either with each other, or with other government economic policies, fiscal policy was not envisaged as an instrument of control over economic conditions. Each government regarded its fiscal action as something determined for it by the economic conditions of the time.

The most skilfully unified fiscal policy on the part of the Canadian governments, can not, of course, prevent such depressions as that after 1929, but it might do much to mitigate their severity. Fiscal action is now significant in the Canadian economy, and if it is treated as a policy it becomes an additional instrument of control, to be used along with the other policies. Since fiscal action was regarded as an accident, and not as a policy, we cannot presume that the deficit financing of the past years ($1.8 billion between 1929 and 1936) was directed at the objects most likely to

stimulate recovery. Canadian governments as a whole, it has been already shown, are spending one-third of the national income. This sum, if directed by one supreme authority, or by co-ordinated fiscal actions on the part of all governments, would represent a great power for influencing the movements of the national income. But since it is spent by different authorities, with local as well as national aims, and with the presumption that their fiscal actions are decreed for them, the power of this sum to influence the course of the national economy is greatly reduced. Nor can we presume that the deficit financing of the depression years even remotely harmonized with the various government economic policies (tariff, monetary, etc.)

It should not be implied that the failure to devise a fiscal policy on a national scale necessarily indicated a lack of statesmanship. The absence of a national fiscal policy may indicate rather that regional divergences in Canada are very real, and that accordingly people are willing to pay a high price for having ten governments, each independently trying to pursue what appears to be its own ends.

It would be an error of analysis to underestimate the importance of regional divergences in Canada, the different regional economic interests, the racial,religious, historical and philosophical cleavages. But these divergences are not constant, and they are apt to find new expression and new emphasis in times of economic difficulty. The first great depression in the 80's and early 90's brought them to the surface,[3] but they were submerged in the subsequent boom from 1896 to 1913. The second great depression after 1929 fostered a recrudescence of the regional movement in Canada, as it did the nationalist movement in many countries. At present, however, it would be optimistic to hope that an external trade

(3) See G. Smith "Canada and the Canadian Question", 1891

boom was around the corner to resolve regional divergences, as happened before. On this occasion, the economic progress necessary to reduce the divergences may require some concerted effort within Canada itself, in the formulation of a national economic programme. In reaching this end, it may still be possible, however, for people to have the satisfaction of possessing ten governments to which they can attach their various loyalties without the country having to forego the important weapon of unified fiscal control, a weapon that promises to become increasingly necessary in the future as Canadian governments as a whole have to try to achieve a balance between social progress and reform on the one hand, and encouragement to private enterprise on the other.

As a result of Canada's financial history, by 1936 about 25% of both Dominion and provincial expenditures went to charges on the deadweight (i.e., non-self-supporting) debt. Apart from the factors which tend to increase the debt steadily, the interest burden tends to remain high for two reasons: (1) Conversion to lower rates is not easy since so large a part of the debt is not callable in Canada, about 44% being callable elsewhere; 12% is callable in any of three centres, and the remainder in one or two centres. (2) The bulk of the debt carries interest between 4% and 5%. Although precise information is lacking, it is open to doubt whether even the Dominion has succeeded in borrowing at a lower average rate on bonds than private industry has through common share financing. Furthermore, the government debt represents the costs of war, settlement, communications and utilities, as well as the costs of aiding private enterprise and of conducting undertakings which private enterprise considered too risky: as such the government debt service has to be met mainly from taxation, and since the government debt contains within it no automatic adjustment to the varying fortunes of the economy, it becomes particularly burdensome in times of depression. As distinct from this

question, there is also another. Experience indicates that the volume of public debt is likely to continue its growth, perhaps sufficiently so as to make the proportion of public to private investment increase. If this should happen, the real costs of the debt would prove more, or less, burdensome according as the increase in public investment was, or was not, bidding away capital from private enterprise. This is another reason why, with the present public debt level and more especially if that level rises, public investment should be "timed" so as not to conflict but rather to move inversely to the ups and downs of private investment.

If the proportion of public to private investment increases steadily, and if that public investment is not nationally co-ordinated to secure maximum efficiency in its use and is not "timed" to compensate for fluctuations in private investment, then the consequent growth in the proportion of fixed interest to equity debt and the periodic bidding away of capital from private enterprise, might render it increasingly difficult for government debt to preserve its gilt-edge character. In other words, if Canadian governments continue their post-war policy of having their fiscal position (and therefore their debt growth) dictated to them by the fluctuations that external trade conditions impart to the economy, it will be necessary for them to make a determined effort to strengthen the sinking fund position, perhaps by building large funds in times of boom, as an alternative to periodic downward revisions of the interest rate (or to its counterpart of moderate inflation).

2. Present Budgetary Position and Future Prospects

Unique view of public finance by business at present

There is no Canadian historical parallel to the present budgetary position, or to the position in which private enterprise finds itself in relation to public finance. At the

conclusion of the War, the sudden increase in the fiscal burden represented a major problem, but expectations were that the "natural" rise in productivity, and an increase in population, would lower the war debt burden just as England had recovered from the effects of the Napoleonic War debt. And in Canada, the boom that began after 1924 seemed to indicate the beginning of the fulfilment of these expectations. The depression after 1929 was a setback, but, it was hoped, of merely a temporary nature. It was only during the recovery from 1933 onwards that increasing realization of the new situation became widespread. The persistence of deficits up to 1936, the changed nature of international trade, the recognition that depressions as well as wars now add greatly to the debt burden, the tendency for tax rates to increase rather than to decrease in the recovery years, all served to bring home the fact that high taxation is likely to become the normal condition in Canada. While it would be unwise to read too much into any sudden change of business men's expectations, it would be equally unwise to neglect the basis on which these new expectations have been founded. In 1936, which was an advanced year of recovery, the national income was still some 30% below the 1929 level. But meanwhile the gross funded debt of the Dominion and the provinces had risen by over 36%, from $4.4 billion to $6.0 billion, the revenues raised had increased by 8%, many of the necessary capital expenditures of the governments that had been postponed in the depression had not yet been renewed, and the stubborn relief costs were not proving readily reducible. While the drought had been an important factor preventing recovery and adding to government charges, the changed nature of international trade was such as to suggest that a sound and lasting recovery in export trade would not be easy to achieve. And if there were any slump in England after the cessation of the armament programme, Canada's export position might be further disturbed.

Even now (August 1938) it seems unlikely that the 1938 national income (in terms of dollars) will rise above that of 1937, and the 1937 level was only midway between that of the depression bottom (1933) and the previous peak (1929). In view of these conditions, there is strong evidence that expectations of fairly high taxation in the future are well founded.

Need to envisage future budgetary problem

It might be felt that any reference to future Canadian budgets should be deferred until some of the more pressing and immediate economic problems have become less acute, or at least until the economic situation that is likely to confront this country in the future is more clearly defined than it now is. But it is not impossible that the questions of financial policy which will arise in the next few years will be at least as difficult as those that are present now, and so there may be some value in trying to foresee the future budgetary problem. Furthermore, any solution that is offered for the immediate fiscal and financial problems must imply some assumptions or pre-suppositions about the long-distance outlook, so that even the discussion of the present-day position requires that some attention be given to the probable future position.

Any inquiry into the probable future position has to be made in the light of the financial history of Canada in the years of economic recovery after 1933. The forces affecting the financial position were such in these years that the Dominion and the provincial governments increased their outstanding debts by $616 million: their combined current deficit in 1936, an advanced "recovery" year, was still above $73 million despite a 44% rise in revenues between 1933 and 1936: many expenditures (both capital and current) that had been postponed in the depression, had not been renewed by 1936. Even in the year 1937, which was more prosperous than 1936, there was only a little closer approach to budgetary balance.

If the economic position that existed in 1937 were maintained for some years, and if the expenditures kept near their present levels, it might be expected that taxable capacity would increase somewhat, as people become adjusted to the idea of higher taxation. In these conditions there might be some small surplus available for capital works, or perhaps even for debt redemption: and if Canadian governments increased their efficiency in expenditure and in revenue raising, the surplus might be larger. But Canada's financial history suggests that certain strong resistances will have to be overcome before the governments will co-ordinate expenditures and taxes in order to improve their efficiency, and that equally strong resistances will have to be overcome before any surpluses that happen to emerge will be used for debt redemption. But given a maintenance of the 1937 conditions, and no tax remissions (although possibly tax readjustments), a position approaching balanced budgets would emerge, with little surplus available for capital expenditures or new services. It would be an equilibrium that would appeal to the tight-rope artist.

Probable future growth of government expenditures

But the above result presumes that there will be no change in expenditures in the next few years, and no significant change in the country's productivity.

It is likely, however, that certain expenditures will tend to rise in the near future. Whether their rise will be counterbalanced by declines in other expenditures is a matter for conjecture.

It is clear that some expenditures that were reduced or postponed during the depression years, have not yet been renewed. On capital account it is to be expected that expenditures on certain public works, including highways in some provinces, will increase in the future and that a substantial amount of deferred depreciation will have to be made good.

In current account, especially in some regions, expenditures on highways, health, education and domain, are still below their former levels, and it is likely that increased attention to natural resources, both human and physical, will require at least the restoration of expenditure on all these items. In addition, for the country as a whole, it is likely that the growing demands for social insurance, particularly for unemployment and for sickness, will tend to provide a new upthrust to the expenditure level. Again, the state of international confidence suggests that Dominion expenditures on defence may be subject to forces that call for an increase. Also, it is not inconceivable that the steady growth of road competition with the railways, especially in some regions, may affect the level of Dominion expenditures on transport. Furthermore, if it should prove to be true that Canada has some redundant capacity in certain of her great export trades, this also would affect the level of Dominion and provincial expenditures, probably on both current and capital account. If the governments met any such situation with their previous policies in this regard, the new expenditures would show themselves as maintenance expenditures (particularly relief), but if they attempted the more positive (and more difficult) policy of industrial and regional transference, the transition would again cause an upthrust to expenditures, probably of greater magnitude in this case as attempts were made to encourage more intensive economic development as compensation for the decline in export trade. The latter policy, although causing greater expenditures in the short run, would however provide some positive stimulus to the growth of national income (e.g. by encouragement to the further working-up of natural resources, etc.) and would tend to be more economic than the mere maintenance of those men and resources that seem to be suffering from more than a temporary unemployment.

"Economies" in government expenditure

Such increases in expenditure as may be expected in the early future, may be compensated by declines in other expenditures so that in fact total expenditure would remain near its present level. And several possibilities exist for securing reductions in certain expenditures. It is not impossible to envisage each Canadian government making efforts towards economy, such as have been made in the United Kingdom on two occasions since the War. It is true that in the United Kingdom these efforts proved to be little more than a temporary check to the steady growth of expenditure. But in Canada it may be presumed that a determined effort by each government to maximize the efficiency of its services would lead to not insignificant economies in expenditure. If the government of the United Kingdom, which has some reputation for efficiency of administration, still considered it worth-while to "take up the slack" on two occasions since the War, it may be presumed that Canadian governments could secure some reductions in expenditures by similar methods. In some Canadian governments, the lack of any efficient method of budgetary control would in itself suggest that possible economies are available. As distinct from this, it is possible that some economy in government expenditure as a whole, some increase in the efficiency of total government expenditures, may be effected by a new co-ordination of services as between Dominion, provincial and municipal governments. If individual or collective governmental efforts at increasing government efficiency were made in the next few years, they might suffice to counterbalance many of the likely increases in expenditure that were enumerated above. Of course, if international trade were to become more profitable in the next few years, one might hope for such a reduction in relief and other "depression" expenditures that total expenditures might even be reduced, for a while at least,

even if the new expenditures contemplated above were made. But any such hope has to be tempered with the knowledge that relief costs proved highly intractable in the recovery years after 1933: and it is well to remember that even with improved international trade, many rehabilitation expenditures on equipment and on people may prove to be necessary. Even given a rise in the national income, some regions may continue to show evidences of distress, and their need for social services and rehabilitation services may be great. In short, an increase in international trade may not yield as great a reduction in the so-called "depression" expenditures as is suggested at first sight, although any improvement in trade would provide some relief to budgets.

Future budgets and future economic position

It is clear that Canada's future economic position would be greatly affected by an outbreak of any European war. If Canada were not among the belligerent nations, a war would probably affect an immense improvement in her economic and fiscal position (including a reduction of external debt). If Canada were outside the fringe of the actual combat, she would likely make the same sort of gains as accrued to the United States in the early part of the Great War, and as accrued to the United Kingdom in the early part of the Napoleonic wars. Canada's economy, and its financial institutions, are fitted to provide many of the sinews of war to the combatants. If Canada were numbered among the belligerents, the effect of a war on her long-term economic and financial position is impossible to envisage.

Apart from the case of war, the future budgetary position will be greatly dependent on the future state of international trade, and particularly so if Canadian governments do not integrate their fiscal policies and add them to the armoury of economic weapons to be used to fend off the onslaughts

that changes in international trade make on the level of Canadian incomes. If international trade suffered fewer restrictions in the early future, some significant increase in the national income might be hoped for. But at present, politics and economics are appearing to become inseparable in more and more countries, and international trade shows little evidence of enjoying increasing freedom in the world as a whole. Indeed the evidence is mainly to the contrary, and the growth of new devices of trade management is already beginning to make the old techniques of tariff adjustment and commercial treaties appear to be rather immature methods of affecting the flow of trade. If these devices extend in operation, the effects on Canada may be far-reaching. But if international trade suffers no more restrictions in the next few years than it now does, Canadian governments still have two distinct sets of problems confronting them, one concerning the shifts that have already occurred in Canada's trade position and which have created more than temporary distress in some regions, and one concerning the problems that would arise in the event of an early recurrence of depression. These difficulties seem to resolve themselves into two dilemmas. One arises in this way. At present, Canadian governments try, so far as they can, to support needy regions. While this course is economically justifiable if the industries or regions are suffering only temporary difficulty, it is less economically justifiable if they are suffering from a decline in resources or a permanent loss of markets. For such conditions wisdom dictates not mere maintenance, but the difficult process of gradual industrial and population transfer. In so far as this problem is not faced, a future depression would further complicate the matter, and add to the number of uneconomic positions that would have to be maintained.

If a trade recession should occur in the next few years, Canadian governments will face a further dilemma. If they act in a negative way, as in the previous depression, there will be deficits, cuts in expenditures, increases in taxation, further unemployment, and further deficits. The downward spiral will be encouraged by the governments' budget-balancing efforts, and their actions will again tend to increase unemployment, add to relief costs and to debts, and to smaller chances of balance. If on the other hand, the governments try to pursue a more positive policy, maintaining or even expanding capital expenditures, refusing to increase tax rates despite declines in revenues, they will again encounter debt increases, probably even on a still greater scale, for a while at least.

Either the negative or the positive policy will result in debt increases. The success of the positive attitude in alleviating the severity of depressions when they occur would depend on the proper co-ordination of fiscal action as a whole, and on the integration of this policy with foreign exchange, banking, and tariff policy. In view of the lack of fiscal co-ordination between governments at present, in view of the failure of their remedial policies to differentiate between permanently and temporarily distressed areas, in view of the fact that Canadian governments have never in the past made enough out of the trade booms (either by way of debt redemption or by the building up of extra-budgetary funds) to assist their financing in the subsequent depressions, and in view of the unbalanced budgets of the advanced recovery years (1936-7) some people may feel uneasy about the probable success of any positive policies.

In the more remote future, the budgetary position may be of considerable significance in this economy, as in others. In the future, demands for social progress and reform are

likely to increase, and budgets will presumably have to try to achieve some balance between social reform on the one hand, and encouragement to private enterprise on the other. Put in other words, the task of governments is likely to become increasingly the task of getting higher revenues without causing undesirable repercussions on the skill and initiative of those who motivate private enterprise. This task may resolve itself into two broad movements.

In the first place, Canadian governments have always found themselves undertaking those works which private enterprise would not or could not undertake. In only a few instances do Canadian governments operate undertakings that yield revenue, notably in the case of liquor control, some power commissions, etc. In the future, governments may have to search for the control of a greater number of revenue-producing undertakings, so that new sources of revenue will be available for meeting the growing expenditures of social reform without involving too heavy taxation on households and firms. Such a movement may prove to be of great importance, for it may be the only compromise which can at once yield the revenues to meet the growing expenditures, and yet hold down, or even reduce, the taxes that are distasteful to private enterprise. In Canada such a movement would involve no change in principles: Canadian governments have always owned enterprises. The only change involved would be that they controlled some more profitable enterprises, as an alternative to the maintenance, or perhaps the steady increase of,taxation.

The second movement that may be expected is the gradual acceptance of high taxation by households and firms. Governments can do much to win the confidence of those on whom the dynamics of the economic system depend, so that they will continue to give their intelligence and determination to enterprise, even if they do have to share the rewards. Probably this confidence can best be won by a determined effort,

on the part of governments, to increase their own efficiency.

Future fiscal action as part of national economic policy

For as long as one cares to look ahead, the Canadian national income is likely to be affected by changes in external trade. In the past, the regionalism of the Canadian economy, and the division of power and lack of co-ordination of fiscal policy inherent in federalism, resulted in an aggravation of the movements communicated to Canada from the outside world. When overseas trade boomed, the governments followed fiscal policies that intensified the boom, and when overseas trade declined government action again tended to increase the oscillation. But a properly co-ordinated system of government expenditures as a whole, and a properly co-ordinated tax system, can if skillfully used, act towards "damping" and reducing the variations in the national income caused by changing conditions in the outside world. And if fiscal policies are used appropriately with other national policies (Monetary, tariff, etc.) then the resultant national economic programme could go far towards insulating the Canadian national income from the far-reaching effects of disturbances in the world of trade. At present, external trade conditions communicate wide changes to the volume of private investment and of consumption within Canada. But shifts in the volume of (co-ordinated) public investment can be used to offset changes in private investment, and shifts in the methods of taxation (e.g. as between taxes that mainly have their source in consumption, like sales, excise, etc., and those that affect largely the volume of savings, like income tax, and especially sur-tax), can be used to offset the changes in consumption initiated by alterations in the external trade position. Accordingly changes in public investment and changes in tax methods, if used at the proper time and to the proper extent, are important weapons for combatting the changes in private investment and consumption consequent on the international trade position. In the same

way, fiscal policy can provide compensatory adjustments for regional (or industrial) "discriminations" caused by the distribution of natural resources, or by the effects of other national policies, like the tariff or the monetary policy.

Today, in most countries, fiscal controls have entered the stage of trial and inquiry. But their use in the Canadian federal system is perhaps impossible at present. It is extremely important however, to recognize that Canada is now the only remaining political federation that is attempting to operate a completely unco-ordinated fiscal system. In the United States, and in Australia, such fiscal readjustments have been made (by financial centralization, loan council, etc.) that these countries now possess in great measure, co-ordination of fiscal actions in the economy as a whole. Canadian federalism alone remains completely disintegrated in its fiscal policy. It may be possible to state the consequences of the Canadian position both in terms of regional loyalties and in terms of standard of living. If the Canadian people require ten independently operating governments in order to satisfy their regional loyalties, then a large part of the price to be paid will be the difficulty of formulating a national economic programme, and the lack of such a programme may be an important determinant of the future standard of living in the country as a whole. Already there are evidences that the Canadian economy will not manage itself. The wisdom of having a coherent economic policy, with also some reserves of policy, to meet the economic and financial problems of today, and what may be the greater ones of tomorrow, is perhaps obvious.

Problems during period of evolution of national economic programme

The views of the Canadian democracy on issues of economic policy are not particularly precise at present, and

the ends of policy cannot be formulated without decisions being reached on a number of questions.[4] Among these, one of the most important is whether Canada wishes to try to continue her great dependence on exports as the dominant method of providing the national income, or whether she would prefer deliberately to increase production for home markets at the immediate price of perhaps a lower standard of living. These questions are for the people and the governments to decide, but since the objectives are not likely to be clearly formulated for some time the period of evolution will be important. During this period, it is hoped that greater clarity can be found on two issues: (1) The economic loss that arises when either private enterprise or government enterprise is trying to do something which it is not competent to do: the extent to which incompetent private enterprise is being supported by the tariff, or other state props, is not known, but it may be important. With respect to state activities, the quality and efficiency of their service, the competence of the civil servants, and their freedom from domination by privileged groups, are important considerations on which additional knowledge is necessary before any judgment can be made about the competency of governments as a whole, and their efficiency relatively to business.

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(4) Some of the more important questions on which decision is required, may be mentioned. Are regional interests in Canada more fundamental than national ones? Is a low, relatively stable income preferable to a high but fluctuating one? Is a large or small population wanted? How far is the democracy willing to go in order to improve its economic position, or is effective action against depression incompatible with the Canadian view of government? What sort of lack of balance in public finance will public opinion willingly accept? Will it permit disequilibrium in the provinces so long as the Dominion balances its budget? Or will it permit disequilibrium in some special extraordinary budget so long as the ordinary budget balances? Will people allow the government to borrow cheaply from the banks, but shrink at exchange depreciation? Does public opinion envisage an economic policy (tariff, currency, fiscal, transport) that would benefit the world at large, or one that would mainly aim at hoisting Canada on the shoulders of other countries?

These are some of the important issues on which there is little precision at present.

(2) The wastes that arise when private enterprise and government are both competent, but are not pursuing the best social ends. Additional knowledge is required about the wastage of resources, the extent to which uneconomic industries (or localities) are being maintained, and the use of privilege for limiting the investment opportunities of others. These issues are far beyond the scope of this paper, but they have nevertheless an important bearing on the present, and the future, financial position. The decision as to economic policy and the scientific study of the most efficient methods of negotiating that policy in the light of the available resources are particularly important in view of the difficult job that now confronts the governments. And it is necessary that people should become accustomed to differentiating more clearly between economic policy, which is a political issue, and the art of co-ordinated administration, which is a matter for experts, boards and the like, acting in collaboration. These questions were less important when frontier expansion was creating general prosperity and apparent progress, when the great dependence on a few exports allowed a high standard of living (that might have to be propped in depression once at least by a 40% increase in national debt), when the resources seemed extensive and the debts involved in preparing for their utilization seemed likely to be productive, and when the different attempts to enjoy the same standard of living as in the United States were more justifiable than at present. The propinquity of the United States has been important in creating a desire among Canadians for a standard of living comparable to that in America - a desire for multiplication of those things that Americans buy, like automobiles, American amusements, air-conditioned trains, to select only a few items from the beginning of the American alphabet. But it is generally recognized that there is a

great economic disparity between the resources and the entrepreneurial capacities of the two countries. And the Canadian attempt to maintain an American standard of living by the sale of natural resources - at best only partially worked-up within Canada - tends to lead to new debt levels on occasions when resources become thin or when external sales of natural products decline. Deficit financing of Canadian governments in such periods has been aimed primarily at maintaining income: seldom has it aimed at promoting new methods of providing national income, at stimulating new entrepreneurial activity, or at encouraging necessary readjustments within the economy. But the present debt levels and the present economic position, considered with the future prospects, seem to call for reconsideration of the habits that have created the present debts, without having at the same time created some more sound income stabilizers than now exist in Canada.

While these matters lie beyond the narrow confines of public finance, they are the ultimate determinants of the financial position. And they have relevance also to the question of the subsidy relationship between the Dominion and the provinces. The provinces' need for revenues cannot be segregated from the question of the whole economic policy, irrespective of how powers and revenues are constitutionally distributed between the governments. If public opinion dictates that economic policy has to maintain all regions in Canada, whether economic or uneconomic, then a subsidy based on the "need" of the region can probably fit easily with the other matters that secure this end. But if opinion is beginning to feel that an economic policy should aim at raising the national income of Canada, rather than concentrate only on raising the national debt, the subsidy then becomes an integral part of a co-ordinated fiscal policy. And if the

Canadian people feel that national economic ends are more fundamental than regional loyalties, then all matters of Dominion-provincial relations can be considered in the light of efficiency alone. The distribution of constitutional powers between the governments would then be based on a purely pragmatic test - on what the most efficient distribution of power is to permit the pursuit of a national economic programme.(5)

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(5) At the time of writing, the public accounts' investigation that was made for this Royal Commission had not reached completion. The studies for the single governments were available, and these have been used in the sections that follow. But the consolidated accounts of the provinces taken together were not completed and to that extent, it has been impossible here to give precision to some of the matters that concern interprovincial, or Dominion-provincial, questions.

Dominion Government

1. Initial Stage 1867 to 1896

At the close of this early period, the foreign investment in Canada - accumulated since before Confederation was about $1.2 billion of which $1 billion was British funds. About nine-tenths of this investment was in government and public securities, and the remainder in railways. This large proportion of government borrowing was both cause and effect of the phase of economic growth through which the country had been passing. The initial requirements for developing a national economy were mainly those public works that would assist the production of Canadian goods and services, and this involved the provision of transport and the equipment of settlement. Such works were technically large, and therefore fitted for government undertaking, or at least government guarantees. Such works were, moreover, a necessary condition for the expansion of private enterprise within the economy, and for the encouragement of home and foreign investment in such enterprise. But until the end of the 19th Century, economic conditions within Canada, and in the world at large, did little to stimulate foreign investment in Canada. Within Canada itself, the history of the Grand Trunk investment created no preference in the minds of international investors for lending to Canada. And in the period from 1873 to 1896, the conditions of world trade as a whole did little to provide either the means, or the will, to promote international investment anywhere, except perhaps in the United States, on any worthwhile scale. That period - known abroad as the Great Depression - was a rigorous one for a new Confederation, more especially since its territories were large in relation to its equipment of communication. An increase in production and in new sources of supply, required an extension of the market (home or abroad), and a preliminary to that was an increase in internal transport and settlement. The limitation of the

overseas market in the depression after 1873 turned attention to the possibilities of expanding the home market in particular. Accordingly, in this initial stage of development, Dominion economic policy was directed first at the provision of transport, and later at the increase of tariffs (the National Policy).

The transportation development was directed mainly at railways and canals, and between 1867 and 1896, these accounted for 83% of the Dominion's capital expenditure, the larger portion being on railways (61%). This expenditure was not spread evenly over the period, but was concentrated in the earlier part, making two peaks of capital expenditure, one in 1873 and one in 1884.

The former peak coincided with the end of a boom in world trade that had pushed up Canada's exports from $53 million in 1867 to $86 million in 1873. The major object of capital expenditure at this time was the Intercolonial Railway, the peak expenditure being in 1873, after which the Intercolonial expenditures tapered off. Between 1867 and 1875 the Intercolonial accounted for over $22 million of the debt increase, or almost 60%. The remainder of the debt increase was attributable mainly to the increased debt allowance to provinces, and to the opening of the North-West Territories.

As the Intercolonial railway expenditures declined after 1873, new expenditures were undertaken on canals and on the Canadian Pacific Railway, but capital expenditures as a whole remained steady, and on a lower level until 1882, the increases on canals being offset by a decline in the expenditures on the Intercolonial Railway and on the North-West Territories. In these years after 1873, ordinary expenditures rose only slightly, the rise being attributable to the increase in provincial subsidies in 1873, and to the increased maintenance and operation expenses on the expanding railways and canals.

The period after the break of the world boom in 1873 was a difficult one for the new Dominion, as its export trade declined. Imports fell even faster and since customs duties formed a large proportion of Dominion revenues (approximately 70%), government revenues also declined. The contraction of capital expenditures, as compared to the level of 1873 (the expenditures in 1875 were only one-third of those in 1873) was designed to check the growth in debt, and to reduce the unfavourable commodity trade balance. The contraction of borrowing reduced imports and further emphasized the fall in customs revenues.

The Dominion tariff policy was altered in 1879, and this produced the second wave of capital expenditures. As remedial measures to meet the depressed conditions, the so-called National Policy was adopted and new emphasis was given to railway construction, the Canadian Pacific Railway being the main project that required completion. As a result of the railway policy, capital expenditures reached a new peak in 1883, and the westward extension of the railway resulted in some speculation, and a short-lived boom. Imports rose significantly as against exports until 1883, as a result of the expansion of Dominion debt after 1879 and the purchase of equipment, and as a result of the boom associated with the railway extension. This rise in imports took place despite higher tariffs; and revenues rose to a peak in 1883. As the capital expenditures tapered off after 1883, and as new Dominion borrowing fell annually to 1887, imports declined again, and tax revenues fell with them. From then until 1896, capital expenditures tended to decline with some regularity, the canals and the St. Lawrence harbours remaining as the main items of expenditure. Although the policy of granting railway subsidies was begun in 1884, the amounts involved were not sufficiently large to counterbalance the decline in capital expenditures.

The previous capital expenditures had doubled the public debt charges, and by 1887 debt charges amounted to \$9.7 million while the tax revenues were \$28.7 million. The growing burden of the debt charge, coupled with the desire to maintain the credit of Canada in the London market, impressed opinion with the advisability of checking new borrowings for government capital expenditures. In keeping with this change of sentiment, there was a fall in the rate of growth of gross debt, and a more modest rate was maintained until new railway undertakings required financing after 1907. From 1867 to 1887 (i.e. to the completion of the early railway building programme) gross debt increased by an average of \$9 million per year: for the next 20-year period to 1907, the increase averaged only \$6 million per year. After the completion of the Canadian Pacific Railway, total expenditure (ordinary and capital) changed little until the economic recovery after 1896 had increased the buoyancy of revenues, and allowed new ordinary and capital expenditures to be undertaken - without significant increases in debt until after 1907.

The history of Dominion finance during the Great Depression reflected the condition of the economy and the attempts of the government to expand that economy. The stagnation of export trade prevented any significant rise in the level of Canadian incomes, although some expansion of manufactures was apparent under the stimulus of the National Policy. The proportion of labour employed in manufactures had increased from 5% to 8% between 1870 and 1890, but this apparent increase in new investment in manufactures was hardly sufficient to offset the effect of the depressed export trade on the level of the Canadian national income. The two short-lived trade booms of 1873 and 1884 had been connected with the Dominion capital expenditures, and although the consequent rise in imports had increased Dominion revenues, the booms had quickly petered out, and seemed to have done little to increase permanent revenues.

It appeared as if the debt charges were tending to become burdensome, and since the good-will of the London money market was desired in order to hold down interest rates, now borrowing was limited after 1887. But the capital expenditures that were undertaken over the period from 1867 to 1896, while they doubled the old provincial debts that the Dominion had taken over, did something to mitigate the effects of the Great Depression on Canada, and did extend equipment and communications in the country as a basis for future expansion.

The fiscal position of the provinces tended to be even less favourable in this period. Their expenditures tended to outrun revenues, and at the Inter-provincial Conference of 1887, it was indicated that a new subsidy arrangement was desirable.(6) In the 90's almost all provinces tried to widen their revenue basis by the introduction of corporation taxes and inheritance duties. The source of most of their revenues (apart from subsidies from the Dominion) was in crown lands, royalties and fees, and the buoyancy of these revenues was dependent on the expansion of staple exports like minerals and lumber. This expansion was not possible until after the recovery from the Great Depression. The new sources of revenue - corporation taxes in particular - depended chiefly on an expansion of home industry, but the National Policy and the Dominion capital expenditures had so far done little more than prepare a good basis for such expansion. And the revenue weapons for catching available rising incomes, like the corporation taxes and succession duties, were still new, while more direct taxes like the income tax were not yet countenanced.

2. <u>The Boom Period, 1896-1913</u>

The sharp rise in international prices that began in 1896 was preceded by a rise in wheat prices in 1895, a circumstance

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(6) In 1870 the Dominion subsidy had been sufficient to cover almost 60% of provincial expenditures: by 1890 the subsidy covered only about 35%.

that foreshadowed the significance of the ensuing boom for the Canadian economy as a whole. In its early phase, the boom was characterized by a steep rise in exports that produced, almost for the first time since Confederation a surplus of exports over imports, and therefore a favourable commodity trade balance. The rise in Canadian incomes consequent to the increased exports left some surplus available for investment (including debt redemption) and for purchasing more imports. Despite the reduction in import duties in 1897, a reduction which Fielding calculated at 10½%,(7) imports did not exceed exports by sizeable amounts until 1903 when foreign lending to Canada (i.e. to firms and governments other than the Dominion) became significant. In the earliest phase of the boom, (i.e. 1896-1902), the rise in Canadian exports did allow Canadians to purchase more imports, and since Dominion revenues depended largely on customs duties, the rising imports produced rising federal revenues. After 1903, when imports began rising faster than exports as a result of the growth of foreign lending to Canada, Dominion customs duties rose sufficiently to yield substantial budgetary surpluses. This connection between the level of Dominion revenues and the level of imports, and the dependence of these imports on the volume of Canada's borrowing, express the fiscal characteristics of the boom period. Ultimately the buoyancy of Dominion revenues depended largely on the foreign borrowing of Canadian governments and industries, and as the borrowing increased, Dominion revenues became sufficiently buoyant to yield surpluses, and to permit new Dominion expenditures (e.g. increase of subsidies to provinces, new capital works, etc.). This sensitivity of Dominion revenues to changes in the value of imports was both the strength and the weakness of the Dominion financial system. So long as the boom advanced steadily to its peak in 1912-13, Dominion revenues became

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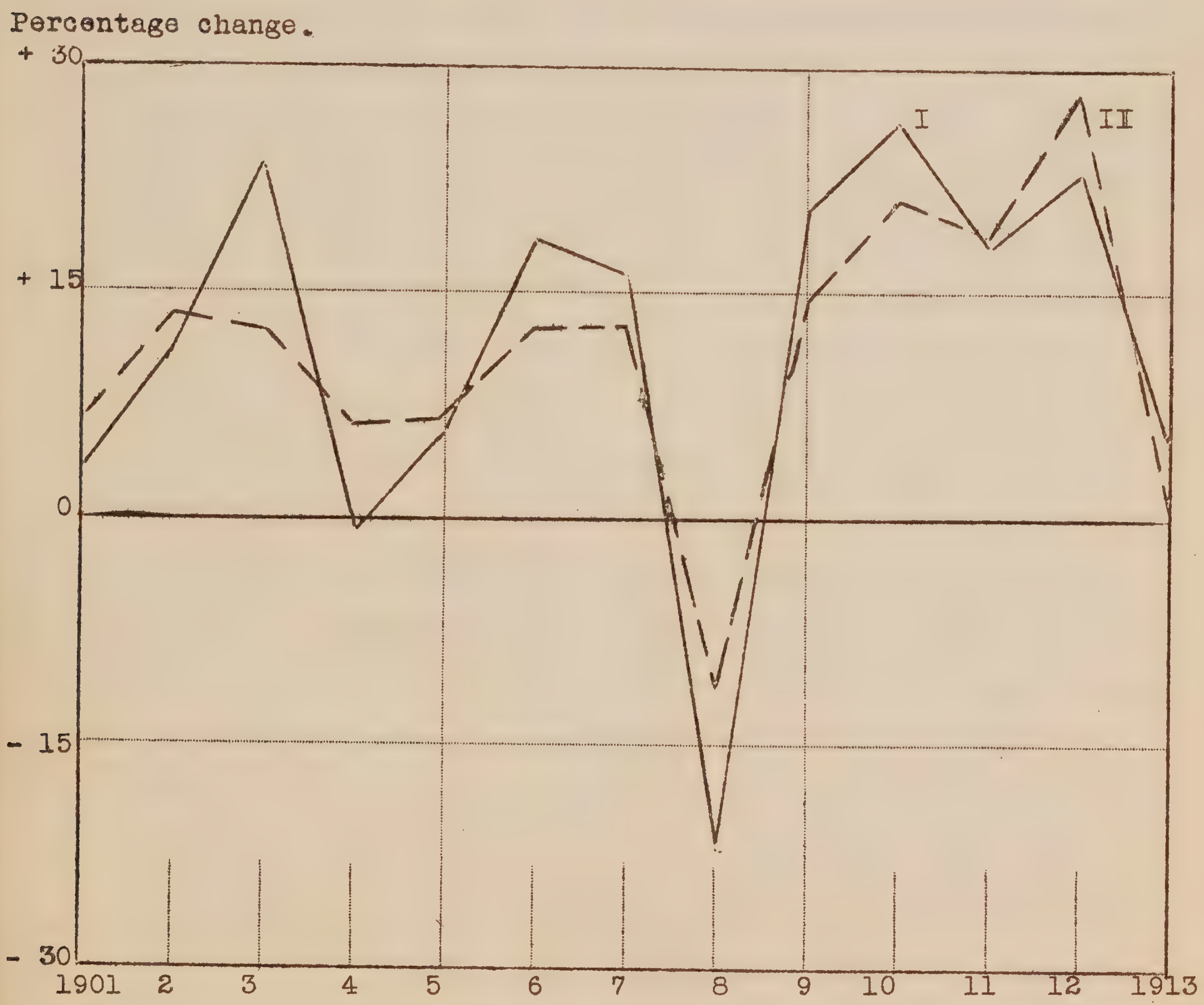
(7) Budget Speech 1900, p. 18.

increasingly buoyant. But, when imports slackened, as happened whenever there was financial stringency abroad (1904, 1907, and 1912-3), Dominion revenues fell proportionately, and the weakness of the Dominion financial system revealed itself just when people thought strength was most required.

The following chart shows the connection between customs duties and imports in the 1900-13 period, and since customs duties were about two-thirds of total Dominion revenues at this time, the sensitivity of Dominion revenues to changes in imports is obvious.

CHART I.

I Percentage change in annual imports.
II Percentage change in annual customs duties.



This chart illustrates the fact that any circumstance that changed the volume and value of imports would change proportionately the main source of revenue of the Dominion government. But this fact was not particularly troublesome in the pre-war boom, and even when the financial stringency of 1907-8 reduced the amounts that Canada could borrow, lowered Canadian imports, and therefore led to a fall in Dominion revenues, no particular reference was made in the budget speech to the narrowness of the tax base, or to the closeness of connection between the level of Dominion revenue and the level of imports. The outstanding feature of the period as a whole seemed to be the buoyancy of revenues, and a temporary decline invited no special comment in 1908.

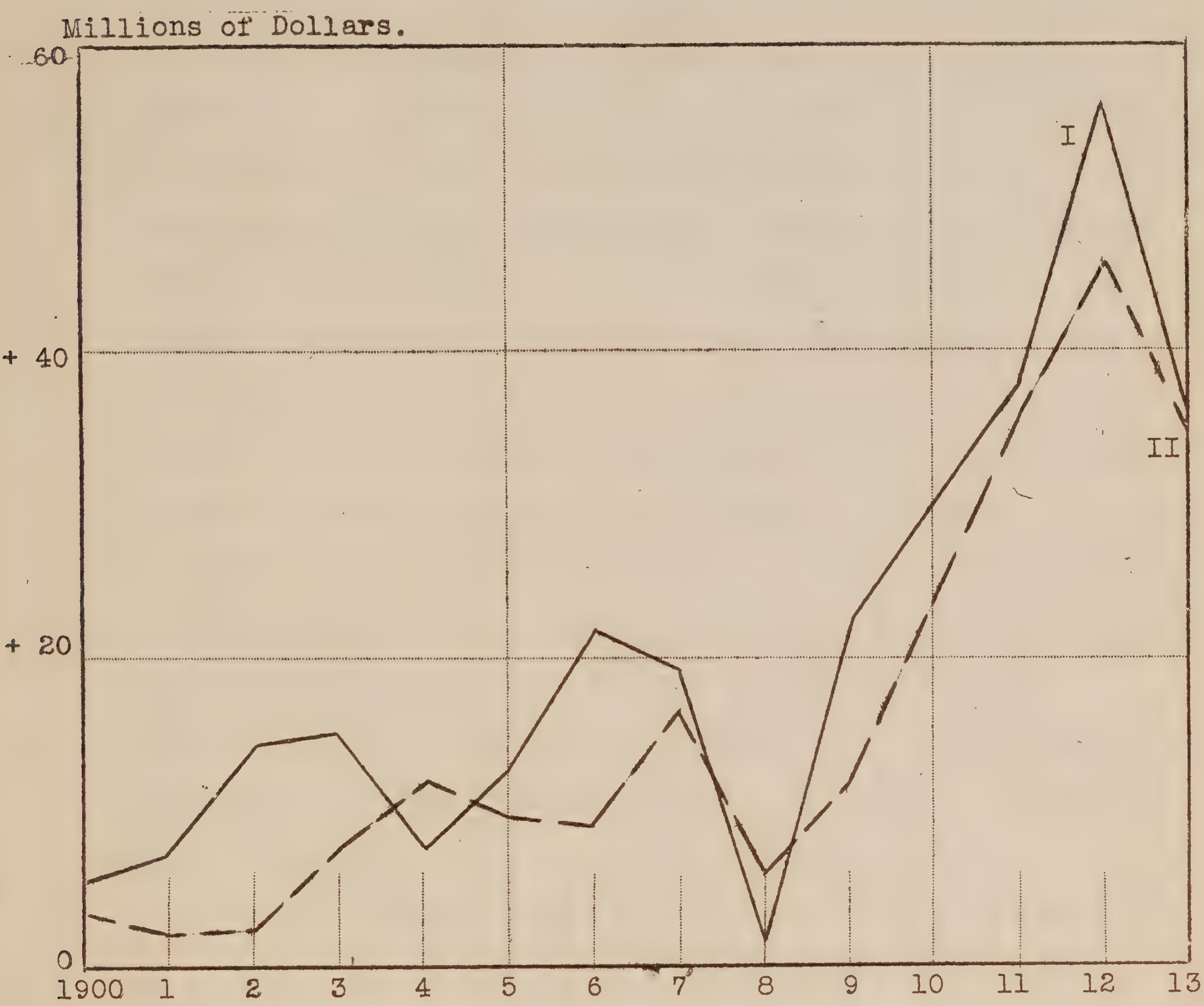
But this buoyancy of revenue was due to two happy circumstances: the fact that foreign lending kept increasing with some progressiveness through the period as a whole, and particularly after 1908, and secondly the fact that although the funds were lent mainly by the United Kingdom, the import goods were purchased mainly from the United States and thus paid the maximum tariff rates. But even if foreign capital had still been available, these happy circumstances were being removed by the very nature of the Canadian boom, which was increasing Canada's equipment and productive capacity, making more and more Canadian goods available to Canadian buyers, and reducing the necessity of importing certain goods. As the process of investment in Canadian primary and secondary industries continued, there was less need to import original capital equipment and primary consumption goods for settlement and settlers, and this was likely in time to affect Dominion customs revenues. But before this effect emerged, the world financial stringency of 1913 caused a sudden drop in international lending, leading to financial stringency for Canada and to a fall in

imports, and these in turn furthered the collapse of the land booms in Canada, reduced inflated capital values, and further reduced Canada's effective demand for imports. The customs revenues immediately reflected the changed circumstances, and the Dominion revenue system indicated the narrowness of its basis. By depending so much on customs duties, and therefore on imports, the revenues were open to wide shifts with every change in the amount that Canada spent on imports. The weakness was revealed therefore before the outbreak of the War, and it was clear that a more satisfactory revenue system would be one that would capture income, as in the income tax, or one that got revenues from what Canadians spent on all goods, as in the sales tax, and more excise taxes. The costs of the War made a broader revenue basis increasingly necessary, and also provided the opportunity for making the change.

The buoyancy of the Dominion revenues in the boom period, and the size of the surpluses to which these gave rise, were important factors in determining the Dominion's willingness to undertake additional expenditures. Accordingly, an attempt has been made here to measure the connection between foreign borrowing, customs revenues, and federal budgetary surpluses in the pre-war period. The excess of commodity imports over exports began rising sharply after 1903 and reached its peak in 1912. This excess may be taken as a rough indicator of the imports that were paid for by borrowed funds. If to this excess, the average tariff rate of the time be applied, the result may be taken as a rough measure of the amount of Dominion revenues that were secured from imports paid for by borrowed funds. The amount so calculated is shown in the chart below. It is interesting to compare this amount with the annual federal budgetary surplus, from 1900 to 1913.

CHART II

I Amount of Dominion surplus on ordinary account.
II Calculated amount of customs revenue due to imports bought by government and industrial borrowing abroad.



There seems to be a fairly close relationship between the absolute amount of surplus and the amount of revenue that came from imports that were bought with borrowed funds. The absolute connection between the annual changes in "borrowed" imports and in the Dominion surpluses, is close. In turn, the extension of Dominion surpluses, especially after 1906, was not unconnected with the expansion of Dominion undertakings at this time. The extension of settlement that was then occurring required additional railways, canals, and post offices anyway. But the size of the surpluses after 1906 was also important in determining the ability and the willingness of the Dominion to

undertake new works. The possibility of meeting new capital works out of surpluses, without appreciably adding to debt, must have affected the Dominion's willingness to extend its public works and its railway programme. Out of the imports that were being "borrowed" by other Canadian governments and by industries, the Dominion was able therefore to secure additional revenues, and to add to the national capital. But in so far as certain new Dominion undertakings, particularly the National Transcontinental Railway, cost far more than expected, the Dominion itself had to borrow to make up the balance. And when international lending declined in 1907-8 and after 1913, and caused a sudden reduction in imports, and therefore in Dominion revenues, the Dominion debt was increased pro tanto, in order to continue and complete the works in progress. The federal capital expenses that had been largely met from customs revenues that were buoyed up by the "borrowed" imports of other governments and of industrial borrowers, were transferred in depression entirely to the Dominion, and were met directly by Dominion borrowing.

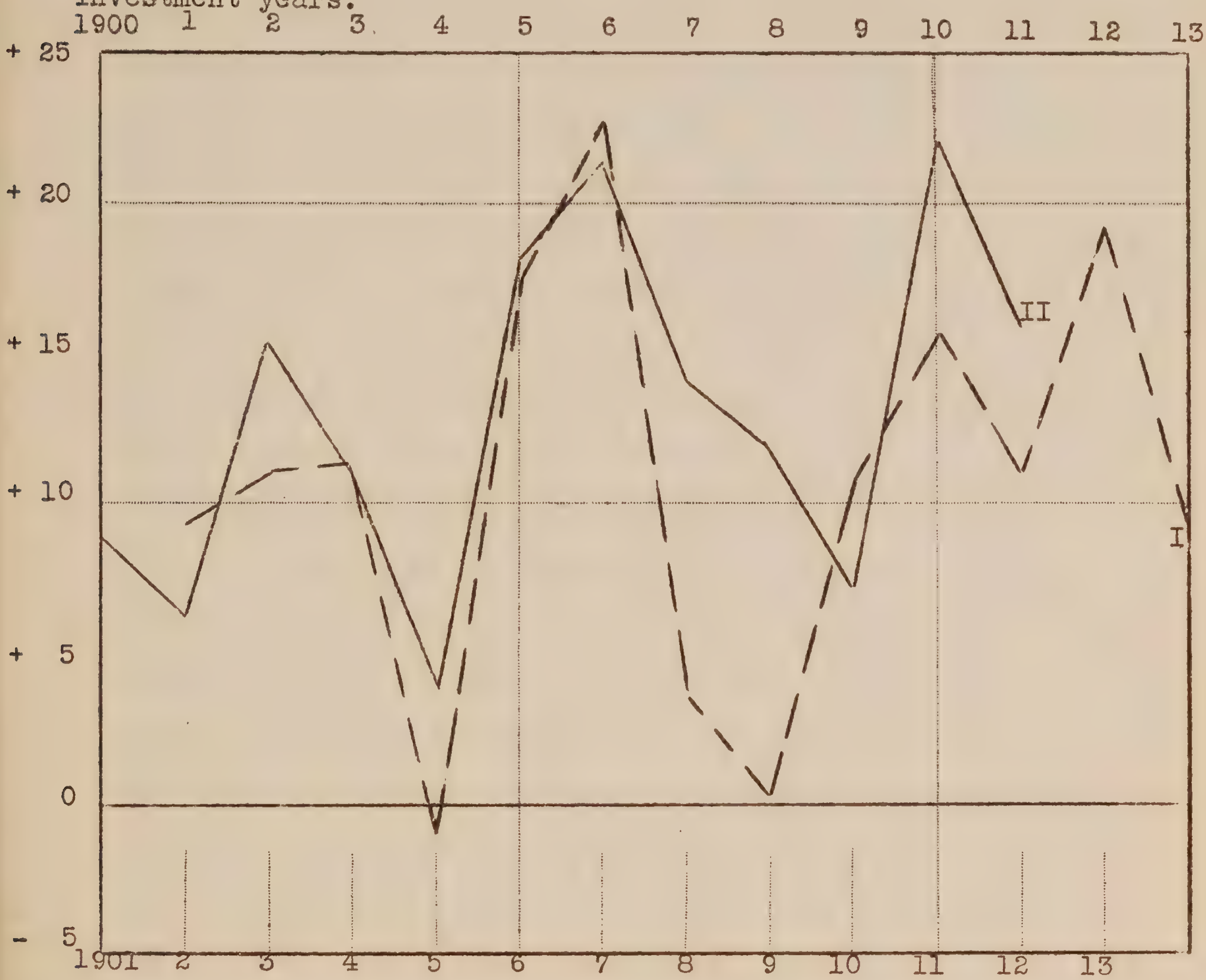
The peculiar character of the Dominion government's fiscal and financial position in this pre-war period is emphasized by contrast with the provincial position. In the early stage of the boom (1896-1902) provincial revenues rose slowly. Although the Dominion had checked its debt growth after 1884 in order to maintain Canada's credit, and although the grant of imperial tariff preferences in 1897 and Canada's ready assistance in the Boer War had all improved Canada's credit and secured the placing of Canadian government securities on the Trustee List (1900), foreign lending to Canada was still modest at the turn of the century, and the Canadian economic indices like construction, bank advances, and immigration, did not show any marked advance until after 1902. The failure of provincial revenues to respond to the initial business upswing

and the growing improvement of the Dominion financial position, were among the topics of the Interprovincial Conference of 1902, which repeated the request of the 1887 Conference for a readjustment of the Dominion subsidy on the basis of population. This request was not granted until the boom had progressed further, until Dominion revenues had become more buoyant, and the constitution of the new western provinces had been settled. By that time, provincial revenues as a whole were beginning to reflect the internal expansion of the Canadian economy. These revenues, apart from the subsidy, came from the domain, from licences and fees, and from corporation taxes and succession duties. The level of provincial revenues, unlike those of the Dominion, was less directly connected with imports, and more directly dependent on the exploitation of resources and on the growth of home industries. The exploitation of resources (timber, minerals, etc.), whether for use in Canada or for export, raised the domain revenues, the royalties, and the licence revenues of the provinces. The expansion of the economy, the growth of railways and other institutions, and the rise in the levels of corporate and private incomes, increased both the corporation taxes and the succession duties. As compared with the Dominion government which found its main source of revenue in customs duties, - on what Canadians bought from abroad, - the provinces found their source of revenue in the volume of business in Canada, and in the income that was derived from the exports of resources and commodities. Of course the provincial revenue systems did not at that time use taxes that would make the revenues vary in direct proportion to Canadian internal economic expansion and to Canadian exports. Nevertheless the following chart shows a close correspondence between changes in total revenues raised by the provinces, and changes in a

measure[(8)] that may be taken roughly to represent the growth of Canadian business and of exports. The changes in revenues lag one year behind the changes in the business condition.

CHART III

I Percentage change in annual home investment plus exports.
II Percentage change in annual revenues raised by provinces.
Investment years.



(8) This measure, called "home investment and exports" was constructed by A. Cairncross "Die Kapitaleinfuhr in Kanada". Welt. Archiv. Nov. 1937, p. 609. While this measure of the level of Canadian income is subject to qualifications, its rate of change may reflect approximately the rate of change in economic conditions during the period.

Dominion revenues, being dependent on imports, were sensitive to the Canadian spending on foreign goods, and their high level at this time was dependent on the fact that much of the spending was done on foreign loaned funds. Provincial revenues on the other hand, were more closely connected with the income that was being derived within Canada, from its home industries and from its export trade. Since provincial revenue systems were not directly based on income taxes at this time, it is not surprising that the relation between provincial revenues and "home investment and exports" (Chart 3) is not more close. Of course, while the provinces as a whole tended to have a broader revenue basis than the Dominion at this time, the financial position of each individual province was dependent very much on its own particular economic position, on its natural resources and on its own fiscal policy, (in particular the form of its tax system).

While the characteristic of the pre-war revenue system was the Dominion's dependence on customs duties, the characteristic of Dominion (and provincial) expenditure was the volume of government investment. This was mainly in the provision of national equipment, principally railways, but also in public buildings and institutions, roads, harbours, and in some provinces power, telephones and other utilities. The nature of the economic expansion, and the nature of the system of federation combined to give the total government investment of the period certain characteristics. Each government, Dominion, provincial, and municipal, within its own sphere, had to reach a decision about the prospects of settlement within its boundaries and about the capital equipment necessary to round out that settlement, and as the boom progressed they became less able to take a "commercial view" of the probable returns from such investment. From the beginning of the boom, the governments' decisions to invest were not always made in

the same way as commercial decisions. The need was to open new areas and to expand the economy, and decisions were ostensibly based on expectations of future "profits" or commercial possibilities. The factor that tended to make the probability of error great was the presumption that the unopened areas contained large resources, able to maintain very large populations, if only the equipment of communication and settlement were provided. And the nature of the economic expansion that was taking place did much to enlarge these long-term expectations about Canada's future. In the early stages of the boom, if over-investment or improperly directed investment did occur, the rapidity of the expansion of the whole economy soon seemed to justify the investment, and created the view that the previous decisions had been made on a sound basis. Since the boom was a long one, and a great one as booms go, more venturesome and bolder investment decisions were taken, and often seemed justified, until in the last phase (1909-12), the nature of the governments' investments was such that the probability of error in the decisions was large. And this was perhaps equally true of private investment at this phase of the boom.

In the pre-war period therefore, there were several strong forces tending to expand the scale of government investment and services as a whole.

(a) Optimism about the resources of the country, which increased in the later stage of the boom (1908-12), led to the desire for a rapid provision of communication and settlement (e.g. railways, telephones, agricultural aids, roads, harbours, schools, hospitals and aids to immigration). Some of these responsibilities rested on the Dominion government and some on the other governments.

(b) The fact that private enterprise could not provide the means to this expansion rapidly, and sometimes not at

all, justified government action on a large scale, on the ground of social necessity.

(c) The fact that the governments were independent, with real differences of interest, induced them to pursue the expenditure policies that seemed best fitted to meet their own requirements. The net result might, or might not, yield a co-ordinated public policy. The investments of one government (e.g. in a railway) might render uneconomic the investments of another government (e.g. in another railway, or competitive highway).

(d) The nature of the government investments also created special conditions affecting the scale of investment. The cost of necessary equipment (railways particularly, but also roads, harbours, institutions, etc.) was very large. In such instances, the choice was between the making of a big investment in the particular work, or the making of practically none at all. The nature of the works made a middle way difficult. And since the economic expansion of the country was rapid, there was a good chance that the new lump of investment would be worth while. And since the alternative - the leaving of the work undone - was politically difficult, such jobs were more often done than left undone.

Then when underlying conditions changed and depression set in after 1913, there was little choice but to complete works in progress. The governments did not have a clean slate to work on. They had to take into account the costs to which they were already committed and the communities established in areas served by the projects half-completed. These considerations dominated the establishment of the national railways during the War, and also affected certain purely provincial undertakings.

By 1913 the Canadian economy had greatly increased its capacity for export: indeed in certain directions the capacity had probably increased faster than the exports themselves. From 1896 onwards, the external debt payments made by governments and private enterprise had increased more rapidly than exports, as a result of the scale of borrowing. Government finance had contributed to this expansion in the manner described above. Buoyant revenues whenever they arose, as they did for the Dominion government after 1906, had not been used to wipe off developmental (or unproductive) debts, but had been "ploughed back" into the Canadian economy, as when the Dominion surpluses were used for new railway construction. By 1913 the Dominion government's balance sheet indicated the extent to which the government had been concerned with developmental expenditures. The outstanding debt was then over $520 million as against $285 million for the provinces as a whole. The significant Dominion expenditure up to 1913 had been on railways, the amounts being as follows:

Railways

($000)

Canadian National and Canadian Government Railways	496,266
Hudson Bay Railway	6,087
Canadian Pacific Railway Subsidies	48,496
Canadian Pacific Railway Advances	39,749
Other Railways	7,639
Total	598,237
Of which written off to Consolidated Fund	91,538

The second item in 1913, much less important, was for public works.

Public Works

($000)

Canals	105,009
Harbour Improvements	21,600
River Improvements	19,836
Docks and Terminals	2,725
Public Buildings	13,278
Miscellaneous	2,487
Total	164,935

The third and remaining item of any size was the expenditure on Harbour Commissions, which in 1913 totalled $30 million.

Other items, like loans (good or bad), were negligible. It is true therefore that at this time the Dominion balance sheet indicated that the major capital expenditures had been almost entirely directed at development, especially extensive development through provision of communications, and that a comparatively large amount of these expenditures had been written off to the consolidated fund. The annual net debt charges were not large, amounting to over 9% of total expenditures. In the ordinary budget moreover, about 29% of the current expenditures went to transport and steamship subsidies; administration of justice, legislation and general government took 21%, defence 10%, post office 10%, provincial subsidies 9%, and the remaining 12% went to domain, agriculture, public welfare and miscellaneous.

Since a comparatively large part of Canada's equipment, especially in communications, had been provided or guaranteed by governments, and since a considerable part of the equipment was only in process of construction in 1913, the breaking of

the boom was bound to involve the implementing of government guarantees, and to impose on governments the costs of maintenance of the new undertakings, which cost might prove large if the previous expectations as to Canada's needs had been over-optimistic. In short, gross expenditures were liable to increase, especially Dominion ones. But the Dominion revenue system still had a narrow base. Customs duties yielded 71% of the total revenue, but their yield was liable to considerable reduction with the decline in borrowing and in imports. Excise duties yielded 14% of the total revenues but they were not elastic. The need for increasing revenue possibilities, for enlarging the revenue from Canadian incomes or from the spending of these incomes in Canada, was revealing itself as the government expenditure requirements increased, and as the capital import boom that had buoyed up customs duties broke down.

3. War Finance

The war period in every country was abnormal, from the economic point of view, and the accompanying change in social outlook was great, so that the ability and the willingness of private enterprise to bear new burdens of taxes, and of households to make great savings for war purposes, permitted a scale of government taxing and borrowing almost impossible in a peacetime economy, even in conditions of boom. In Canada, as in the other belligerent countries, the government was slow to raise the tax levels after the outbreak of the War. This was partly because Canadian opinion did not yet feel that the War would be of long duration, and partly because Canada entered the War in a period of depression that made new tax efforts difficult. For these reasons alone, a significant change in the Dominion revenue system was difficult to achieve at the beginning of the War. Furthermore, any attempt of the

Dominion to pluck more revenues almost certainly involved some poaching on the revenue sources that had been the provinces' preserves. And any such attempt seemed likely to involve new tax instruments that would prove costly in a short war. Accordingly in early 1915, the most obvious method of increasing Dominion revenues was to raise customs duties (7½%), and to borrow from the United Kingdom for essential war purposes and for the completion of the Canadian railways.

As the War advanced, however, all the factors that affected taxation and borrowing in Canada altered their bearing. As Canadian war expenditure increased and as war debts mounted, it seemed likely that the Dominion would require larger revenues in the future, so that the establishment of new tax machinery would fill a permanent rather than a temporary need. Again, as the War continued, the trade depression gave way to recovery which increased national income and therefore the amounts available for taxation or government borrowing. The War served to increase the demand for Canadian exports, mainly of food and munitions, and by the autumn of 1915 orders for munitions reached $600 million, almost half the pre-war capacity of all Canadian manufactures. This, combined with a good wheat crop, brought a substantial measure of recovery. As the economy as a whole was moving on to a war basis, and as the War itself quickened, psychological change was increasing the citizens' willingness to make sacrifices. These conditions made the prospects of a Canadian war loan brighter as the year advanced and the first loan was floated with success in November, 1915.

The success of this loan was important psychologically in England as well as in Canada. It was floated in the period of recovery after the 1913 depression, and the Canadian national income was still low as compared with the levels to be reached at the peak of the war boom (1917) and in the post-war boom

(1919). But in November 1915 income was rising with the favourable export position; prices were rising more rapidly than costs; the Canadian government met the overseas costs of the War by borrowing in London, and American lending was beginning; all these conditions increased investment in Canada, while the enthusiasm for sacrifices and thrift allowed a higher proportion of the income to be saved and devoted to war loans. These factors were all present to make this first Canadian loan a success. As the time passed, British lending ceased, and when the United States entered the War borrowing from that source also ceased. But by that time, the rise in Canadian incomes was great enough to allow still larger government loans, and in 1917 and in 1918 the favourable merchandise balance was sufficiently great to allow Canada even to export small amounts of capital.

The first loan (1915) paved the way for the great Victory Loans that were to follow during the critical years of the War. They educated the Canadian public to the use of investment securities, extended the machinery for investment within Canada, and indicated the possibilities of Canada's reliance on her own resources for borrowing. Indeed so rapid was the change from Canada's pre-war borrowing position, and so surprising was the realization that Canada possessed appreciable investible funds of her own, that the emphasis on a loan rather than a tax method of war finance may have been pushed too far. The government's early financial policy was mainly to promote and foster national savings in the war boom. Resort to increased taxation was not really made until the public indicated its desire for heavier taxation during the year 1917. It is true that a Business Profits War Tax had been imposed in 1916, but it covered only large firms and absorbed one-fourth of all profits in excess of 7%. In 1917, however, the government gave expression to the public sentiment for increased taxation by making the profits tax more drastic, and by imposing the Income War Tax Act. Had the early war loan

been less successful, the government might have found it necessary to be a little ahead of public sentiment in the matter of increasing taxation. The rise in national income from 1915 onwards had increased the taxable capacity of the country as well as its ability to save.

By the spring of 1917 the growth of expenditure needs also helped to induce a change in Dominion financial policy. The prospects of America's entry into the War indicated the probable closing of the remaining source of Canada's external borrowing. The Canadian railway problem was beginning to emerge, because, although traffic was still increasing, railway costs were rising, and the Dominion was faced with the responsibility of taking over half of Canada's railway equipment. In the March budget, it appeared that war costs then amounted to more than \$533 million, while the public debt increase in the same war period was \$543 million. The Dominion was entering the fourth year of the War with few of the war costs yet met by taxation. Accordingly, the Business Profits War Tax was steepened, but the Finance Minister indicated that the institution of the income tax seemed inadvisable. But within three months' time, the crisis that was developing in British finance indicated that the Dominion would have to extend all its financial operations, both in taxation and in Canadian loans, and accordingly the Finance Minister stated that the time had arrived when "we must resort to this measure". By thus introducing the income tax, a significant step was taken towards the broadening of the Dominion's tax base, and the government was preparing to take fuller advantage of the public's willingness to make sacrifices. With respect to borrowing, methods were also improved: treasury bill financing increased, and a thrift campaign was pushed to try to ensure that the first Victory Loan (November, 1917) would have a more popular appeal than the previous loans. The introduction of the \$50 bonds, and more instalment payments were also designed to have this effect. Both in size and in

distribution this loan was a success, almost one person in ten in the population subscribing. The bulk of the loan, as of previous ones, was taken up by large interests, particularly insurance companies and industrial companies.

In this critical year also, the Dominion increased its note-issue by $50 million, reducing the gold backing of the issue from 62% in January to 42% by December. This currency dilution was justified later by Sir Thomas White on the grounds of financial necessity, and also on the ground that the steep rise in the price-level could absorb this increase in currency.

The subsequent financial history of the war period involved a furtherance of the new tax and loan policies instituted in 1917. On the taxation side, the Business Profits War Tax had its rates increased by the lowering of exemption levels in 1918, and by alteration of rates in 1920. In 1921 it was removed. In 1918 the income tax was altered by reduction in exemptions, and by increases in rates in the higher income brackets. The income tax was amended considerably in 1919 by steeper rates, and in 1920 a surtax was added on incomes over $5,000. In that year also the sales tax was introduced at 1%. On the borrowing side, the second Victory Loan was launched in 1918, and the volume of small bonds ($50 and $100) was comparable to that in the first Victory Loan, but since the second loan was larger than the first, the proportion of small bonds declined. The third and last Victory Loan was floated in 1919, and the amount subscribed was somewhat similar to that in the previous year.(9) By then, the proportion of small subscriptions had fallen still further.

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(9) The amounts subscribed in the three Victory Loans were $546 million in 1917, $681 million in 1918, and $620 million in 1919.

The third Victory Loan is distinguishable from the two earlier ones mainly by the fact that it was made subject to income tax, whereas the earlier ones had possessed tax-free privileges. These privileges had been given on the grounds of expediency - it was a case of no tax on the bonds or else a higher interest rate, according to Sir Thomas White.[10] On the other hand, since the war boom had created many large private incomes, and since the recently instituted income tax was graduated so as to tap these incomes, there was a distinct possibility that owners of such incomes would turn their wealth into these securities to escape the tax. And the possibility of such legitimate tax evasion would remain, in greater or less degree, according to the relative level of the income tax and the rate of progression, until the last of the tax-free issues were recalled. In the second place, the issue of tax-exempt government securities made "government" investment especially attractive to those investors who could best afford to invest in equities. Those persons whose wealth is sufficiently great to allow them to diversify their equity holdings and thereby spread risks, could not afford to invest in equities so long as tax-exempt bonds could be bought.

The War, by improving Canada's export trade, had greatly added to the national income. Had Canada been neutral, and had the increased income been used, not to purchase more imports, but to repay the debt incurred in the pre-war boom, there would have résulted a considerable improvement in Canada's external debt position. But the war boom did not permit a debt reduction; its stimulus went to war consumption purposes almost entirely. Accordingly, at the end of the War, the Canadian economy was faced with the need for repaying most of its pre-war (especially railway) debts abroad, and with the need for making money transfers within Canada from producers to those

(10) Monetary Times, August 31, 1918.

who held claims on the state for their war sacrifices: in addition, since certain Canadian outputs had been enlarged to meet exceptional war demands, some agricultural and industrial readjustment would be necessary. Agricultural and industrial equipment, much of which had been enlarged to meet a temporary war demand, carried a particularly high rate of depreciation. (The period of readjustment in agriculture was likely to be longer than in manufactures. The demand for many manufactured goods would cease with the close of hostilities but it was likely to take some years before Europe restored her agricultural acreage to pre-war levels, and until that occurred, the European demand for the agricultural products of other continents was likely to be temporarily high.)

The significant change in the Dominion financial position as a result of the War, is to be found in the new level of debt charges. Net debt charges by 1921 exceeded the total expenditures of 1913: pensions alone amounted to about 40% of the 1913 expenditure level. The outstanding changes in the balance sheet were as follows:

	1913 ($000)	1921 ($000)
War	-	1,684,513
Government shipbuilding	-	57,288
Soldiers' Land Settlement	-	78,293
Loans to foreign governments (part-interest bearing)	-	7,578
Canadian National and Canadian government railways	496,266	1,830,012
Hudson Bay Railway	6,087	20,624
Public Works	164,935	258,363
Total outstanding debt	520,837	3,520,039

The changed debt situation (exactly $3 billion increase between 1913 and 1921) was attributable mainly to the War, but the railway problem now reflected itself in the Dominion balance-sheet, the Dominion having been compelled during the War to take over and operate the two bankrupt systems. The above changes in the balance sheet illustrate, therefore, not only the effect of the War itself, but also the effects of pre-war railway policy and war-time fiscal policy. As we have seen, it was not until 1920 that the Dominion tax base was fully broadened, and by that time economic conditions were not such as to permit large tax yields. As a result, war financing had been very much a matter of government borrowing, more so than if it had been possible to take full advantage of people's willingness to bear sacrifices. In wars, governments tend to ask of some citizens full sacrifice of their physical strength, but of others they ask only small sacrifices of financial strength, and this fact is not unconnected with post-war demands for pensions, social services, etc., on the part of those who have risked more than wealth. As a result of delay in requiring financial sacrifices during wars, governments in post-war periods are heavily indebted to bondholders, and find it difficult to justify moderation in grants of social and other services. These conditions were not peculiar to Canada. But they were added to other peculiar Canadian conditions that created budgetary as well as economic difficulty. The war boom had done little to reduce pre-war indebtedness, and in part this showed itself in the railway indebtedness in the Dominion balance sheet. But the budgetary difficulty was unlikely to be only a matter of the new Dominion debt structure. The necessity of economic readjustment within Canada was likely to add to the budgetary problem. In Canada, as in other countries, it was post-war, rather than war finance, that was troublesome, and this difficulty only emerged when the period of borrowing or

inflation ended. The subsequent deflation which appreciated the holdings of the new mass of rentiers, at the same time increased the frictions that were present as the economy tried to adjust itself from war to normal requirements. The more difficult this readjustment, the greater was the budgetary problem, for not only was taxable capacity lowered by declines in employment, but new expenditures emerged in increased railway deficits and relief. Some of these costs of industrial readjustment were likely to lead to demands for new services for which provincial governments were responsible, and if their revenue possibilities were limited, they also might seek federal aid. On several sides, therefore, the Dominion financial position was likely to be rendered difficult at the end of the War. Moreover, its expenditure needs were likely to grow and its revenue possibilities to decline as deflation proceeded and the Canadian dollar appreciated in terms of the pound sterling. The broadening of the base of the Dominion revenue system towards the end of the War was not likely to prove only a temporary necessity.

4. Post-War Dominion Finance

As already indicated, the post-war financial position was dictated largely by the pre-war one (debt position of the economy as a whole and over-expansion of railways) and by the war finance (its extent, and the emphasis on loans as against taxation). But the post-war period was characterized by more than a mere enlargement of the scope of government finance. It was characterized by significant changes in overseas countries as buyers of, and competitors with, Canadian goods, and by changes in the framework within which the Canadian system of private enterprise operated.

The extent to which government finance had increased its importance in the economy is evident by the fact that by 1921 20% of the national income was taken in taxation for

government services (i.e. all Canadian governments), and well over 5% of the national income went to debt transfers, somewhat over half of this amount being for external debt.

The extent to which other countries had been affected by the War did not reveal itself immediately. The decline in England's financial position, in her ability to import goods and export capital, and the strengthening of the United States position in the same respects, was evident fairly soon after the War. But the full extent of the financial weakness in Europe, the growth of industry in non-European countries (including the U. S. A.), the desire of these latter to protect their new industries, and the eventual counterpart of this in the growth of European protectionism, especially in the rush for cover from the 1931 depression, were all factors affecting Canada's export position, although their full significance was not revealed until the second Great Depression (i.e. after 1930).

The change in the framework within which the Canadian system of private enterprise operated may be indicated by considering the framework as of three parts.

(1) The psychological factors that determine the household demand for goods, the prevailing ideas about the functions of the state, international economic relations, etc.

(2) The technical factors that determine the productive methods available, and applicable to the country's resources.

(3) The institutional factors, including the nature of the state, the nature of the principle of private property, the monetary and banking mechanism used.

Each of these factors was modified to some extent by the War, its costs and its effects. There was a change in the social organization, and that change affected the operation of the economic system, which in turn affected the expenditures of all governments as well as their tax possibilities. But while most countries experienced similar changes, the effect in Canada was heightened by a special circumstance. In Canada

after the War, the slowing down of the rate of economic progress was an important contributor to the change in social philosophy that was taking place. The War had increased the number of private Canadian fortunes, and the decline in the rate of economic progress had aided the process of social stratification. The rate of economic progress was no longer the solvent to most social problems. Indeed the pre-war rate seemed to have added to social and economic problems, partly by its provision of a volume of equipment sufficient for a very large population, and partly by the addition of the young immigrant "block" to the population. The consequent distortion of the Canadian age structure led to different sets of social problems at different times. As the children of the immigrant "block" came to school age, the educational equipment (particularly in certain provinces) had to take care of this peak, and there were unused educational facilities in certain regions as the children moved into occupations. Then occurred a period when employment opportunities for young people were insufficient to meet the demand. The 1931 census indicated the emergence of this problem, and the form it was taking.(11) In the future, the age-distribution of Canada's population will result in an old age "block", with effects on the volume of old age pensions.

But the effects of the post-war change in the rate of economic progress became apparent only slowly before the depression. The war boom had concealed the fact that other countries were likely to increase their output of competitive goods (particularly wheat), and that Canada's conjectural resources, rather than those that were known and exploited, had been important in creating optimism with respect to her economic future. Nevertheless the gradual emergence of certain social problems in the post-war period indicated a change in Canada's rate of economic progress.

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(11) Census 1931, Vol. 1, p. 278 for age-distributions in occupations; p. 201 for age-distributions in provinces.

This change combined with the effects of the War to alter the psychological, technical and institutional factors in Canada's economy.

On the psychological side, the War quickened the growth of the social conscience, reflected in the enlargement of the social and welfare services of the state. New services came into existence and older ones were enlarged. In Canada, these lay mainly on the provincial (and municipal) governments, and affected their debt and tax levels during and after the War. As already mentioned, there is some indication that the enlargement of social services is connected also with the increasing stratification of society: that because of the nature of the distribution of wealth, citizens near the margin of subsistence have come to be considered deserving of special state aid, or services free or at less than cost. Anyway, in the post-war period, Canadian governments devoted increased expenditures to the main risks to which labour is prone - risk of destitution through unemployment, sickness or old age - as well as to the provision of certain other services at less than cost. In the depression, the provision of these services and of relief became a national problem, and had to be met from Dominion as well as provincial and municipal revenue sources. But apart from depressions and the deficit financing associated with such periods, the tendency towards expansion of social services raises at least two important problems in financing. (1) If social services are financed by taxes that increase the costs of producers, this increase, even if slight, may affect the volume of output, or even the competitive position of producers, especially in international competition with countries that do not have such services or that for other reasons are in a stronger position than Canada. If taxes for social services do produce this result, there is danger of a vicious circle being created - new services adding to taxation, which may

curtail output and employment, and require further extension of services. (2) If the social services lie mainly on local governments (provincial and municipal), then the less prosperous the region, the more are local industries affected by the additional taxation. Only a few areas have sufficient control over prices of their goods to enable them to pass taxation on to consumers in other areas. The less fortunate economic regions are seldom in this position, and social services, growing with their economic misfortunes, may add a cumulative handicap to their local industries. Thus if economic retardation is very marked in some regions of a country, it may happen that the areas most needing social services are those least able to provide them.

On the technical side, the War altered the framework of the Canadian economy, mainly by the enlargement of output for war demands - wheat, munitions, certain manufactures, lumber, etc. In addition, the War served to prop certain industries that had expanded to meet the pre-war boom, industries that were threatened with collapse when that boom ended. Their collapse was postponed until the post-war depression (1921). In all these cases, readjustment was necessary, and Dominion and provincial financial aid to the localities and individuals affected was somewhat analogous to war pensions. But in some industries, particularly wheat growing, readjustment took time. European wheat acreage did not recover its pre-war level til 1926, and even then the accident of poor European yields and the stimulation of consumption by the world boom through 1927 and 1928 hid the necessity of full Canadian readjustment of acreage till after 1929.

On the institutional side the War had striking effects on the state, the banking system and private property. It produced greater intervention by the state in the economic system, more centralized banking management, and a modification of the individual's right to full use of the fruits of his labour and

wealth. (In general, the larger the income the greater the modification.)

Changes in the Canadian monetary system (i.e. relaxation of currency and banking restrictions) began on the first day of the War. Although the banking system restrained itself in investing in government securities, the emergence of a domestic bond market, the institution of the Finance Act, and the growing mass of governmental obligations all affected the structure and the operation of the monetary system. In the post-war period in Canada, as in the other belligerent countries, there remained a mass of governmental financial obligations that represented, not internal or external trade indebtedness, but largely the claims of those who had lent their labour or capital for war purposes, claims for an annual share of the current returns from industry and trade. Finance was no longer the handmaiden of industry alone. It had to serve both government commitments and industrial needs. And there are signs in Canada, as elsewhere, that there has been a decline in the demand for that type of service which banks formerly delighted in - the provision of working capital by short-term loans. Hence banks as a whole have been free to take up more of the government debt than they might have otherwise,(12) while the general public and industrial companies, the latter having grown in average size, have provided more of the working capital of industry and commerce. As a result of the new levels of government activity, particularly the new government function as an agent of transfer of funds to creditors (home and abroad), the post-war banking systems have had to give new attention to management of currency and to governmental requirements, and consequently new banking techniques have been evolved (open-market policy, short-term balances and latterly exchange equalization). In most countries that lacked a central bank, the need for one was indicated at the Genoa Conference (1922). The creation of the

(12) Since public opinion has apparently accepted the new level of government financing that has been done by banks in the past few years, it would be interesting to know what further government interventions would be sanctioned in the same way.

Canadian central bank, however, did not occur until financial difficulties in the depression after 1929 further emphasized the importance of government finance and monetary policy in the Canadian economy. Since the creation of the central bank, the Canadian monetary mechanism has so changed that monetary policy has become a causal factor of new significance in future economic change.

The fact that government debts, expenditure, and taxes took an increased share of the national income in the post-war period involved some change in social organization that is not without significance in the operation of private enterprise. Of the total tax system of the Canadian governments as a whole, only a part - although an increasing part - is proportioned to incomes and profits. But the total tax system, whether it lies on costs, or whether it is in part shifted to prices, to lower wages, or even to reduced employment of labour, has in the last few years, become increasingly regarded by producers as a burden. The additional taxation that arose during the war period was regarded largely as an emergency measure, and in the good business years from 1925 to 1929 the reduction of Dominion and most provincial tax rates seemed to bear out the hope that the war taxation levels had been temporary. The increases in taxation in the depression years (1931-3) created further disturbance, but then again, this period was considered abnormal. But now, after several years of economic recovery, tax rates have increased[(13)] rather than diminished, and since a further depression might involve still higher rates, households and firms now generally realize that high taxes are likely to persist and perhaps even to become "normal". Accordingly, the question of the present and future influence of taxation on the incentives to investment is of more importance than at any

(13) e.g. Dominion surtax and corporation taxes raised in 1935: corporation tax and sales tax further raised in 1936.

previous time. It is true, of course, that governments transfer large parts of the taxes levied to bond-holders, to those receiving services free or at less than cost, and to other government purposes, so that a large part of the state expenditure again enters the income stream of private households and firms. (The question of how large a part of taxation re-enters the income stream, and particularly the incomes of those on whom the volume of investment depends, is of fundamental importance, and will be discussed later.) It is true also in a liberal-democratic state that governmental financial action as a whole must have some dependence on the desires of the people as a whole. Nevertheless, the individual taxpayer (whether household or firm) regards state action, not as being determined by him, but as a determinant that, among others, affects the cost of the goods or services he buys, and also the level of income remaining to him for consumption and saving. And these considerations increase in importance if the economy is in a condition of recession or depression. The modification of the principle of private property, towards the idea that the state can absorb an increasing share of the returns of labour and enterprise, can be accepted willingly by the taxpayer only when he agrees that the post-war social organization necessitates this sharing of current income with the state. Accordingly, the task of getting higher taxation out of a community, without causing repercussion on enterprise, is in part the task of managing human nature so that those on whom the dynamics of the economic system depend will continue to give their intelligence, determination, and skill to enterprise, even if they do have to share the rewards.

Unfortunately wars, and now also major depressions, carry government expenditures and taxes to new levels comparatively quickly so that there is not always time for willing acceptance of the new government action by taxpayers. The immediate reaction

to a sudden raising of the level of state action, particularly in taxation, may induce firms to try to bolster existent economic positions by regulation of prices and quantities, or by attempts at such regulation.

By 1921 the Dominion revenue system was broader and deeper than before the War, particularly in taxation. The following table indicates the change:

	1913 ($000)	1921 ($000)
Customs duties	104,691	105,687
Excise	21,452	36,755
Sales Tax	-	61,273
Manufactures, stamps, etc.	-	12,383
Corporation Income	-	38,864
Other	-	2,328
Business Profits	-	22,816
Income Tax on persons	-	39,821
Miscellaneous	1,335	396
Tax Revenue	127,478	320,323
Total Revenue	148,101	359,386

Both before and after the War, the tax revenues amounted to about 86% of total revenue. In the tax revenues, the change from the pre-war dependence on customs duties is marked. These duties varied little in amount as between the two depression years 1913 and 1921. There was a slight increase in the yield of excise duties, but the remainder of the tax system was due to the innovations during the War; in 1921, the new taxes yielded 55% of the tax revenues.

On the expenditure side, the significant changes are indicated in the following table:

	1913 ($000)	1921 ($000)
Net Debt	12,213	152,488(a)
Pensions	94	53,688
Transport	37,851	42,772(a)
Government	27,237	47,235
Defence	13,812	17,381
Subsidies	11,280	12,212
Domain	7,707	11,914
Post Office	12,822	30,447
Welfare, Education and Agriculture	8,176	13,208
Total Expenditure	131,192	381,345

(a) Interest on Canadian National Railway issues, included in net debt charges, $36,337,000.

The growth in debt, pensions, and transport is significant. The transport and net debt charge items include the railway deficit of $50 million in 1921, but this item was liable to decrease with economic recovery. Net debt, pensions, and transport had formed 38% of 1913 expenditures, but 65% of 1921 expenditures. Although all items of expenditure had grown, the old Dominion functions (government, defence, subsidies to provinces, and domain) had fallen in importance: in 1913 they combined to account for 46% of the expenditure, but by 1921 they amounted to only 23%.

As compared with provincial and municipal expenditures, the Dominion outlay had grown more rapidly after 1913, as a result of the War and the transport costs. But expenditures by other governments also grew appreciably between 1913 and 1921. While the Dominion outlay rose by 191%, the provincial rose by 87%, and the municipal by 131%. As a result, by 1921, the total tax collections of all Canadian governments amounted to an appreciable part of the national income, calculated at approximately 20%.

The actual distribution of this expenditure of government is difficult to summarize, but it may be roughly indicated. In the depression year 1921, the Dominion and provincial expenditures might be summarized as follows:

(1) Payments to those Canadians to whom the governments were indebted (internal bondholders and pensioners). This item was probably the largest of the transfers from taxpayers to other Canadians, and may have amounted to one-quarter of the total government expenditure.

(2) Expenditures on behalf of all citizens through certain services of government (governing, legislation, justice, post-office and defence). This took probably one-quarter of total expenditures.

(3) Expenditures directed mainly at the benefit of citizens in certain areas by means of public works and transport, - about one-fifth of total expenditure.

(4) Expenditures for the benefit of future citizens, in education and natural resources management, - less than one-tenth of total expenditure.

(5) Payments to those getting social services, - less than 5% of the total.

(6) Payments to foreigners to whom Canada was indebted: the amount of debt being paid externally may have amounted to about 15% of the Dominion and provincial expenditures. This amount represented a real deduction from Canadian incomes, whereas the preceding items represented a transfer of national income within Canada.

The above distribution characterized a depression year just at the end of the War. In the boom years, the transport payments would be smaller by reason of the smaller railway deficit. In depression years, as social philosophy moved on towards greater diffusion of welfare services, the significance of that item would also change.

The new level of government expenditures as a whole was not likely to remain unchanged after 1921. Apart from the effects of depressions on expenditures and revenues, the trend of expenditure as a whole was likely to be upward. The change in the rate of economic progress, the necessity for taking greater care of both human and physical resources, the need for capital works, in railroads, highways, utilities and other physical forms that might appear likely to stimulate regional enterprise, all indicated that expenditures would tend to rise for governments as a whole. Between 1921 and 1930 provincial expenditures on current account increased by 106%, and Dominion expenditures by 10%. In the Dominion, however, the trend had tended to be downward until 1926. In the provinces, which had incurred new debts for highways, utilities, and public works during the 20's, net debt charges rose; at the same time new public welfare services, and additional attention to provincial domains, tended to push up provincial expenditures with some degree of regularity after the War. The Dominion however managed to reduce its debt charges: the expenditures on railway deficits fell rapidly, especially in the 1925-8 boom years: pensions declined to 1926, and the general financial position permitted some steady decline in Dominion taxation after 1924, beginning with a

reduction in the sales tax from the 6% level to which it had been stepped up in the post-war depression years. But although Dominion expenditures appeared to be more amenable to contraction than those of the provinces as a whole, and although the Dominion did manage to secure a small reduction in its outstanding debt between 1925 and 1928,(14) its financial position was dominated by much the same forces as were affecting the provincial budgets.

The expenditure needs and the revenue possibilities of all governments were associated with the level of national income. If it rose, expenditures on railway and other utility deficits declined and welfare needs tended to fall, while at the same time revenues became more buoyant. But the level of national income depended in turn very much on the Canadian export position. Thus when foreign trade improved between 1925 and 1928, the increase in Canadian employment improved the railway position, lowered certain other government expenditures, improved revenues, and even permitted new expenditures on public works of different sorts. The latter tended to add to the magnitude of the boom. When foreign trade was depressed, as in 1920-1 and 1929-30, the opposite condition held. The reduction in trade and employment added to railway and other utility deficits, added to welfare expenditures, led to increased taxation, and tended to reduce expenditures on public works. In the post-war depressions, therefore, Canadian governments as a whole, by their fiscal actions, tended to reduce their own investments, and to spend more on utility deficits and on welfare. Because so large a part of the nation's physical capital was owned (or guaranteed) by governments, depressions added increasingly to the normal post-war budget problem: and since social philosophy was changing, depressions added to welfare costs and introduced a further element of budgetary difficulty.

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(14) It fell from $3,575,419,000 in 1925 to $3,491,648,000 in 1928.

If governments met these difficulties by contracting their own investments in Canada, or by creating tax systems that did anything to hinder private investment, they were likely to discourage the exchange of goods and services within Canada - an activity which is something of an alternative to exports as a provider of national income. Accordingly, in the post-war period, when new levels of government activity were reached and showed a tendency to rise further in depression, any failure to recognize the influence of fiscal policy on Canada's home trade might nullify the other national efforts that were being made to try to maintain income by strengthening the international trade position, (e.g. by tariffs, trade agreements, or exchange policy, if resorted to).

The importance of fiscal action as a factor affecting the extent of private investment in Canada, may be roughly indicated by the fact that government expenditures as a whole amount now to about one-third of the national income. The direction of these expenditures, their distribution to different purposes and localities, is important in directly affecting the direction and the volume of home trade. The method of raising the funds by taxes (or taxes plus deficits) is both directly and indirectly important in affecting the level of investment. So far as deficits involve new bank credit, they are directly expansionist in their influence. So far as taxes are raised in the ways least likely to add to costs, they are indirectly important as creating the least possible disturbance to private enterprise. If the revenue methods are ill-considered, their adverse effects on private investment may offset whatever beneficial effects accrue from the governments' expenditures as incentives to investment.

The question of the effect of taxation on investment is not readily answerable, but several features of the relation of high taxation to enterprise have to be borne in mind. At

any particular time, it is not easy to define a 'high' tax. Some taxes which were considered onerous in the pre-war period are no longer thought so: others that appear heavy in depressions become unimportant in booms. And this raises the question of the psychological affect of taxation, a matter which tends to be of prime importance at present, since, as we have argued earlier,(15) there has been some recent realization that the present tax levels are liable to persist. The expectation of the maintenance of the present tax-levels, or even the fear that recent additions to government debts are likely to increase future taxes, may prove to be more effective in delaying private investment than the fact of the taxation itself. Unfortunately, the present tax method; and recent tax history, do little to minimize the effects of taxation. The loosely knit nature of the tax system as a whole, the tendency for much of the structure to be on industrial costs rather than on returns, and the habit of raising these taxes without discrimination in depression periods, suggest that the Canadian tax system as a whole is not calculated to produce the least disturbing effects. In depression, or in areas suffering economic retardation, the additional taxation created by these adverse economic conditions, discourages investment. As a factor amplifying the periodic swings in the Canadian economy, reducing its burdens in booms, and adding to them in depression, the Canadian tax system is no longer insignificant.

With respect to expenditures, it has been already indicated, that the post-war tendency has been to reduce the governments' expenditures on investments (public works, capital maintenance, conservation of resources, etc.) in depressions, and to add to them in booms. Like taxes, this part of fiscal action has also tended to exaggerate the swings in the economy, and to make the latter more than ever dependent on a favourable export position. It is a commonplace that the Canadian

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(15) p. 44.

economy is dependent on exports. But the extent to which the fiscal action of the governments has added to the Canadian booms that a favourable export trade created, and deepened the depressions that ensued from international trade dislocation, has not always been given proper emphasis.

With respect to another group of expenditures, a similar unfortunate circumstance may arise. That portion of the taxation which goes to internal debt holders (individuals, banks, etc.) has usually been assumed to re-enter the income stream immediately, so that the transfer from taxpayers to bondholders, and from them back to business, is quickly effected without economic disturbance. But since taxpayers give up certain consumptions (or savings), it will be necessary for bondholders to utilize the funds for consumption or savings in order to prevent internal trade disturbance. Some of the internal debt payments are probably spent when received, and re-enter the income stream without creating disturbance. The remainder, which is saved, is the part that may create disturbance. If the external trade condition is favourable, and is stimulating Canadian industries, the funds that are transferred to government bondholders are then readily available for use in the investment opportunities in both home and foreign trade industries. If, however, external trade seems to be declining, and Canadian home trade is lagging or depressed, the funds that are transferred to bondholders may be saved, pending new investment opportunities. In these conditions, the funds transferred to the bondholders are likely to be available only for credit-worthy borrowers, and in view of the economic conditions, only governments may appear credit-worthy. In such conditions, when trade seems to be declining, the transfers to bondholders who save, will in themselves do nothing very positive to stimulate investment, or to compensate for any reduced consumption that has resulted from the payment of taxes

to meet this debt interest. Thus the post-war level of internal debt has been another important factor contributing to the swings in the economic system. Canadian governments as a whole made no positive, concerted effort to expand public investment, on those occasions in which private investment began to lag, occasions in which the investible funds became more available for governments than for private enterprise.

In depression, it is true, the money rates of interest may be lowered directly by banking policy, or indirectly through the actions of the private investors. But if private investment is lagging, this action will result mainly in raising the prices of gilt-edged securities, in revealing the willingness of investors to invest only in government securities. And even if there is some reduction in money rates for private borrowers in depressions, this reduction may not be sufficient to counteract the business man's low estimation of the profit possibilities, until some evidence exists that the depression is about to give way to recovery.

Accordingly, in the post-war period two sets of forces impinged on the Canadian economy. On the one side was the long-term change in position due to the change in economic progress, and coupled with this was the new level of government debts and welfare services. The economic structure required gradual and careful remedy, and the financial structure, with its new level of commitments and of taxation, also merited readjustment. On the other side was the short-term position dictated primarily by the profitability or otherwise of the export trade. When that trade was satisfactory many of the long-term factors ceased to exert their influence. The upswing that good overseas trading produced was a solvent to both economic and financial difficulties: revenues became buoyant, tax rates became unimportant, debt transfers encouraged the boom and deficits declined. But when overseas trade was depressed, then the long-term factors renewed, and sometimes even increased, their influence.

These conditions suggest that appropriate government action would have been directed at the twin elementals; the gradual improvement of the long-term position and, since that position was sensitive to disturbance, the taking of measures that would at least try to prevent short-term movements of external trade from creating too extreme fluctuations within Canada itself. These two problems were different in kind, the former calling for careful improvement of the efficiency of both the economic and the financial system, and the latter requiring expansionist measures to meet temporary external trade disturbances. Since some discussion of these matters was raised in the Introduction, it is sufficient here to indicate that an economic and fiscal policy to meet either the long-term or short-term disturbances was not forthcoming, for reasons already given. Indeed no conscious fiscal policy existed, to meet either the structural or the cyclical needs. The governments as a whole regarded their fiscal position, not as a determinant of investment and intensive development of resources, but as something dictated to them by the economic position of the moment, and that position in turn was dependent, in such circumstances, on the export trade. Expenditures, taxes, and deficits varied in response to external conditions. When these conditions yielded prosperity (1925-8), certain deficit expenditures fell (on utilities, etc.), revenues became buoyant, and governments felt able to make new expenditures or to reduce taxes. In depressions, the opposite held. But although governments seemed to regard their fiscal position as being determined for them, it was nevertheless directly - although not as a conscious policy - affecting the level of investment. In booms, new government investments and reduced taxation stimulated the incentives of private enterprise to invest. In depressions, the curtailment of governments' direct investments, and the raising of taxes without discrimination,

did nothing to encourage private investment, or to maintain total investment. Fiscal policy, it must be emphasized, has a new importance in the economic system when government activity as a whole forms so large a part of the national income. In short, the fundamental problem of Canadian government financing in the post-war period was rather a question of the relations between government as a whole and industry, than a question of financial relations between the Dominion and provincial governments. If any region suffered retardation in its export trade, its government financing would prove difficult, and might lead to claims for assistance from the central government. But if foreign trade as a whole suffered, all governments were likely to find expenditures increasing and revenues decreasing: in such a case the fundamental question related to the cause of the general difficulty, namely the fall in national income. In the present recovery from the depression, with the further disturbances to international trade that have followed from the emergence of "war economies" overseas, the maintenance of Canadian income may prove to be largely a matter of inducing home investment. If that be so, an important function of public finance is to direct government expenditures as a whole so as to stimulate investment, and to re-allocate taxes in a way that will least deter private enterprise. Dominion-provincial-municipal financial relations form a part of this wider issue. And it has to be asked whether the constitutional distribution of powers and revenues as between the different governments ought, or can, be so arranged as (1) to increase the efficiency of expenditures and taxation (i.e. yield maximum benefit for the given expenditures, and raise the revenues with the minimum of disturbance to enterprise), (2) to provide when necessary a national fiscal policy as an additional instrument of economic control, to be used together with banking, tariff, and transport policy when severe disturbances are about to affect the Canadian

economy. To the extent that this is possible, fiscal policy may be another device (or compromise) by which public authority can co-operate with private enterprise. But if there is no conscious fiscal policy on a national scale, then at the present levels of government costs, the fiscal practices of the different governments may hinder, rather than aid, private enterprise, and may offset whatever economic advantages accrue from other policies that aim to increase the returns from foreign trade or home trade.

The history of Dominion expenditure and tax changes in the post-war period indicates that the Dominion fiscal position was dictated mainly by the economic conditions ruling from year to year, and that fiscal action was limited to what prevailing economic conditions seemed to permit. On current account, the post-war depression produced a series of deficits, the 1925 to 1929 boom a series of surpluses, and the years from 1930 another sequence of deficits. In the boom years the surplus rose steadily to a peak in 1928 (year ending March 1929).(16) Thereafter, as a result of the new depression expenditures on railway deficits, unemployment and farm relief, wheat bonus and relief advances, the deficits rose rapidly in 1930 and 1931 and remained high to 1936.(17) The capital account indicated the tendency to enlarge investments in the boom years and to contract them in the depressions. When revenues and surpluses were buoyant in good years, new undertakings were more readily undertaken, and unfortunately tended to reach their maxima just near the peak of the boom. Dominion capital expenditures rose from $9 million in 1925 to $190 million in 1929. This public investment added to the magnitude of the boom. When the boom broke, the

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(16) The current surpluses from 1925 to 1929 were approximately $45 million, $78 million, $84 million, $112 million and $67 million in 1929.

(17) The current deficits, including depression expenses, from 1930 to 1936 inclusive, were approximately $74 million, $151 million, $145 million, $124 million, $108 million, $152 million and $75 million in 1936 (year ending March 1937).

the government had to resort to borrowing for the investment being undertaken, aiming to contract these works as quickly as possible. Capital works were reduced from $190 million in 1929 to less than $10 million by 1934, thus reducing the government investment in the critical period of decline in private investment. The tax history revealed the same passive fiscal policy, tax rates being increased in the post-war depression, reduced in the boom years and increased from 1931 onwards. Taxes were raised (by all governments) in the years that were difficult for private enterprise, and reduced in the years when private enterprise was optimistic. In its fiscal activities, the Dominion tended to intensify, not to offset, the fluctuations that external trade was imposing on the economic system. It was still true, of course, that the total financial requirements of the Dominion government varied inversely with economic conditions. In the boom years borrowing was unnecessary: indeed there was a slight reduction in outstanding debt. From 1929 onwards, the volume of deficit financing was large, and to some extent this offset the factors making for decline in the economic system by maintaining the consumption of those on relief, or in distressed areas. But while deficit financing in the depression helped to sustain the national consumption (especially of necessities), the fact that all governments rushed for new revenues, and curtailed their public investments, was probably as great a deterrent to private enterprise as the increased government spending on consumption was a stimulus. As such, fiscal policy as a whole was not unified, while the relation between fiscal policy, and other national policies (e.g. exchange policy, tariffs, etc.) was only dimly considered in their common bearing on home trade.

Considering post-war Dominion finances in more detail, and considering first the tax history of the period, the outstanding characteristic was perhaps the tendency in the

decade after the War, to return to increased dependence on customs duties. As we have seen, the effect of the War was to necessitate a broader revenue basis for the Dominion. In 1913, of the tax revenues 82% had come from customs duties,(18) while by 1921 only 33% of the tax revenues came from this source. But from 1922 onwards, customs duties became more significant again, until by 1928 they produced almost half the tax revenues (47%).(19) In the recent depression, their proportion fell again, and in 1936 they accounted for only 22%. The mounting proportion of customs duties to total tax revenues up to 1928 is partly attributable to the fact that the economic recovery from the immediate post-war depression involved increased purchases of imports. The recent depression involved a curtailment of imports, and in 1936 the value of dutiable imports was about $500 million below the boom level: consequently there is a ready explanation of the fact that customs duties in 1936 were about $100 million under their 1928 level. To some extent, then, customs were a changing proportion of tax revenues according to economic conditions. But changes in Dominion tax rates after the War also contributed to the growth in the proportion of customs to total taxes up to 1928. In 1922 some changes were made in income tax exemptions. In 1924 the sales tax was reduced from 6% to 5%. As the boom progressed through 1926 to 1928, the tax reductions were even greater in the non-customs tax group.(20) In 1926 the income tax exemptions

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(18) In 1913, tax revenues were $127 million, of which over $104 million were provided by customs. In 1921 tax revenues were $320 million, of which $106 million came from customs.

(19) In 1928 of the total tax revenues of $396 million, $187 million came from customs. In 1936 customs amounted to only $84 million out of a tax revenue of $387 million.

(20) The taxes other than Customs Duties were, in order of importance (1925), the Sales Tax, Excise Duties, Corporation and Personal Income Taxes, and miscellaneous taxes on manufacturers, importations, stamps, etc.

were raised and rates cut: the corporation income tax fell from 10% to 9%. In 1927 the sales tax was reduced to 4%. In 1928 it was again reduced from the level of 4% to 3%, and the income tax was reduced. Corporation taxes were lowered from 9% to 8%. In 1929 the sales tax went from 3% to 2%, and certain minor taxes were repealed (taxes on cables, railway tickets, etc.,). In 1930, the sales tax reached 1% and certain adjustments were made in income tax allowances. The net result of all these reductions in the non-customs group was to counterbalance the effect of the boom on the buoyancy of these revenues. Despite the boom, all the revenues, except customs, remained very constant, as this table of Dominion tax revenue shows.

	1925	1926	1927	1928	1929
	($000,000)				
All taxes except customs	200	205	209	209	200
Customs duties	127	142	157	187	179
Total taxes	328	347	365	396	379

As a result of the tax reductions, especially in sales tax, income and corporation taxes, such buoyancy as the Dominion revenues showed in the boom was entirely due to the customs revenues. The other revenues were remarkably stable, despite the fact that the national income rose by some 26% between 1925 and 1929. Had the taxes on sales and on income not been reduced, their yield would probably have increased in something the same proportion as national income, perhaps by $50 million between 1925 and 1929.

The result of this growing dependence on customs duties was the same as in the pre-war period. When depression came and imports fell, revenue tended to fall in proportion. Accordingly, in 1929, the cessation of the growth of imports and the fall in customs duties was immediately reflected in

total revenues. The reduction in the sales tax in 1930, and the fall in imports pushed tax revenues still lower, so that in 1930 they were 25% below the 1928 level. The upward revision of taxes began in the latter half of 1930, and in 1931 the sales tax was raised from 1% to 4%, and special excises imposed. In 1932 the income tax was raised, the sales tax increased to 6%, and some miscellaneous taxes imposed. In 1933 the corporation tax was again raised, this time from 11% to 12½%, and exemptions removed; in the income tax on persons also, certain exemptions were removed. Despite these changes, it was not until 1933 that total tax revenues ceased their decline, so significant was the effect of the constant fall in customs duties on the total tax revenues. By 1934, however, the effect of rate increases in other taxes, and the measure of economic recovery, combined to increase the revenues from the taxes other than customs.(21) by 37% over their 1930 level. The increases in surtax in 1935, the raising of the corporation tax rate to 13½%, continued this process and the 1936 increase in sales tax to 8%, along with the increased corporation rate of 15% further developed the non-customs revenues. In 1936, these taxes produced about one-half more revenue than in the 1929 boom, whereas the national income was almost 30% below the boom level.

With respect to expenditures in the post-war period, the distinctive characteristic on Dominion current account was the new level of net debt charges (41% of total expenditure in 1925) and of pensions (14%). The proportion of expenditure that was controllable in the post-war period was small. Net debt charges, pensions, subsidies, and other small uncontrollable

(21) Dominion Tax Revenues

($000,000)

	1930	1932	1934	1935	1936
All taxes except customs	166	184	228	244	303
Customs duties	131	70	77	74	84
Total Tax Revenues	297	254	305	318	387

expenditures, had formed only 18% of total expenditure before the War, but averaged between 50% and 60% after the War, becoming much higher when the depression added to net debt charges, railway deficits and relief costs. Apart from these, certain other expenditures were so difficult to control as to be virtually in the uncontrollable class. The railway deficit was determined by economic conditions, as were also relief costs. In short, the "normal" Dominion budget in the post-war period had within it so large a proportion of necessary, or uncontrollable expenditures, that parliamentary sovereignty might be said to have been confined to the distribution of only a small residue. And in the background stood always the threat of new necessary expenditures if economic conditions proved unfavourable; railway deficits would automatically increase, and, according to the nature of the unfavourable conditions, other new expenditures might also be necessary.

In capital spending, the position was similar. The government had always been concerned with the provision of national equipment, and the establishment of the national railways increased this concern. The capital requirements of an extensive railway system, apart from modernization, are fairly large and stable from year to year. The capital equipment for canals, harbours, docks, rivers, etc., is in the same category although smaller in amount. But unlike many of the ordinary expenditures, these "investment" expenditures could be postponed for a short time if the government wished to reduce its total expenditure, the wisdom of such postponement being a matter of policy. Accordingly, the fixity of so large a section of the ordinary expenditures left the "investment" expenditures, and a small part of ordinary expenditures (like government, etc.,) as the only controllable items. If revenues remained fair, all

expenditures could be handled: if revenues rose, extra expenditures could be made on investment, or on debt reduction: if revenues fell, attempts to balance the budget would require a cutting of the controllable items (mainly capital expenditures, and a part of ordinary expenditures).

But the fluctuations in the controllable expenditures were likely to be even greater than the fluctuations in revenue, because as national income rose and yielded more revenue, the rise was accompanied by smaller railway deficits so that more funds would be available for capital expenditures or debt redemption. In depression, as national income fell, the uncontrollable expenditures increased (by railway deficits, welfare, etc.,) so that the controllable expenditures ("investment" particularly) had to be greatly curtailed.

In the 20's, ordinary expenditure tended to contract until 1926 as a result of reductions in debt charges, in railways and canals, in pensions, and in defence costs (to 1925). At the same time, expenditures on railway deficits were contracting as the economy recovered from the post-war depression. However, in the boom period ordinary expenditures rose, partly as a result of enlarged expenses on government, on welfare (introduction of old age pensions), on public works, canals and marine, on defence, and on the special grants to the Maritimes. Net debt charges continued to fall, as did the railway deficits. As a result expenditures (excluding railway deficits) which had amounted to $331 million in 1921 ($381 million including railway deficits) had fallen to $314 million by 1926, and had risen again to $336 million by 1928. By 1929 however, the "depression" expenditures began, showing themselves first in the increase in the railway deficit. As the same time, some new commitments on public works, agriculture, marine, and the Maritime Freight Rates Act were tending to push up the level of ordinary expenditures.

In 1929 and 1930 special payments on reparations and on the Manitoba subsidy raised the year's current total. But ordinary expenditures were cut from $378 million in 1930 to $341 million in 1933. During these depression years, the net debt charges rose by $41 million, so that the reduction in other expenditures was somewhat greater than the fall in total indicated. At the same time (1930 to 1933) old age pensions rose by almost $7 million, the police service by $2 million, and mines service by $2 million. Despite these increases, total ordinary expenditure fell by $37 million between 1930 and 1933, the chief reductions being in defence ($10.4 million), public works ($7.8 million), post office ($7.0 million), and maintenance of government buildings ($6.4 million): in short, the main reductions were in the postponable expenditures (particularly renewals and replacements of capital works). Between 1933 and 1936, expenditure rose again by what it had fallen in the three previous years (i.e. by $36 million) but the increase did not restore to their former level the services that had been cut. Defence alone increased to near the 1930 levels. Public works, government buildings, etc., remained only a little above the depression low. The increases in total expenditure were due to a new level for old age pensions, for defence, as indicated, and for small additions to many items - pensions, agriculture, post office, legislation, buildings, etc.

But while total ordinary expenditures were in 1936 near their 1930 level, the expenditures made on "depression" services raised the actual current expenditures as a whole considerably above the 1930 level. The following table indicates the position.

Fiscal Years ending nearest Dec. 31st.

	1930	1931	1932	1933	1934	1935	1936
				($000,000)			
Ordinary expenditures	378	364	344	341	349	362	377
"Depression" "	41	111	100	95	109	151	140
Total current expenditure	419	475	444	436	458	513	517

The special expenditures associated with the depression have kept high since 1930. In 1933 they reached 22% of the total current expenditure, and in 1936 were 27% of the total. Their significance lies in the fact that they have tended to rise with the economic recovery from 1934 onwards.

These "depression" expenditures may be broken down as follows:-

Fiscal Years ending nearest Dec. 31st.

	1930	1931	1932	1933	1934	1935	1936
				($000,000)			
Unemployment and Farm Relief	4.4	38.3	36.7	35.9	60.7	79.4	78.0
Wheat Bonus and Stabilization	-	10.9	1.8	-	-	(a) 22.6	-
Write-off to Relief Advances to Provinces	-	-	-	-	-	-	18.5
C. N. R. Deficit(b)	35.7	61.0	60.8	59.0	48.4	47.4	43.3
Steamships, etc.Deficit	1.3	.8	.6	.5	.2	1.3	.3
Total special expenditures	41	111	100	95	109	151	140

(a) In the following year the Wheat Board refunded $8 million.

(b) Including debt charges.

In the earliest phase of the depression, the C. N. R. deficit was the outstanding special expenditure. It has tended to decline with the economic recovery. But the effects of the drought, the agricultural depression, and certain special circumstances affecting the numbers unemployed, have tended to keep up, and even increase, the relief expenditures during the

recovery years. These special circumstances compelled the Dominion government, despite its cuts in ordinary expenditure, to continue its financing by means of deficits, even in the economic recovery years.

The following table indicates the deficit position in the depression years.

	1930	1931	1932	1933	1934	1935	1936
				$ Million			
Revenues	345	324	299	312	349	361	442
Expenditures	419	475	444	436	457	513	517
Current Deficit	74	151	145	124	108	152	75
Capital Expenditure	102	53	17	-1	9	17	6
Over-all Deficit	176	204	162	123	118	169	80

The increase in current expenditures, as already indicated, was rapid after 1933, mainly by reason of the depression and drought expenditures. Revenues rose fairly steadily, and with some rapidity in 1936 as a result of changes in the sales tax and in corporation income taxes. In 1936 customs revenues were still about $100 million below the boom level. The 1936 rise in revenues managed to reduce the current deficit, which except in 1934, had kept fairly near the 1931 level.

This table indicates the reduction in capital expenditures during the depression years, a reduction which exceeded that in the provinces. The main constituents of the capital expenditures were:

	1930	1931	1932	1933	1934	1935	1936
				$ Million			
Railways	69.6	30.5	7.4	-9.3	-1.1	9.6	2.8
Public Works	22.0	10.8	7.3	5.8	6.6	6.2	3.1

Among public works, capital expenditures on canals were cut from $9.8 million in 1930 to negligible amounts by 1936. Docks and terminals were cut likewise from $3.1 million, public building expenditures from $2.7 million, harbour improvements from $1 million and miscellaneous from $1 million. The only service still receiving attention in 1936 was river improvements.

The Dominion financial history since 1930 has shown certain inherent characteristics that are worthy of notice. These may be summarized as follows:- the large proportion of uncontrollable expenditures in the normal post-war Dominion budget: the tendency up to 1929 to rely increasingly on customs duties for Dominion revenues: the rapid transition in the financial position when boom gave place to recession, necessitating new levels of Dominion expenditure on railway deficits: as recession gave place to depression, additional commitments were necessary to help governments in the exposed areas: these new expenditures greatly curtailed the Dominion's investment expenditures on capital works.

The events of the depression have removed some of the inherent difficulties, but have added others. The events of the depression have helped to strengthen the tax machinery, particularly in the matter of income taxes, and have increased the proportion of revenues that have their source in income, rather than costs, although increases in the sales tax have served to maintain the share of total revenues that lie directly on costs. Again, the depression involved considerable reductions in the demand for durable and postponable goods - houses, equipment, etc., - and directed attention at the part played by such expenditures in the revival of home investment. The question of government policy with respect to investment has been more clearly formulated than before.

The events of the depression have however induced certain long-period economic changes that seem likely to add to the budgetary difficulties of the Dominion government. On the one side, the depression has created forces making for increased economic nationalism abroad, and as an exporting country, Canada is likely to be affected by these changes over a fairly long period. Certain resultant regional distortions in the Canadian economy may persist for some time, and may necessitate larger expenditures in certain areas, or for certain purposes (e.g. expenditures on welfare, education, labour transference, or government investment, according to the particular policy adopted). Again, certain expenditures that are regarded as special "depression" expenditures are likely to persist, even if national income rises considerably. It is likely that certain welfare expenditures will persist (e.g. unemployment insurance), and if such insurance schemes be formulated, not only for unemployment, but for old age, sickness, etc., expenditures may be permanently affected, and the financing of such schemes, if it is carried out by special taxes on payrolls, might add to the already high taxes on marginal costs. In addition, it is likely that road competition with railways will increase in the future, so that the railway deficits of the past few years cannot be regarded as entirely due to depression; given full economic recovery, road and rail transport competition may be intensified, and this will affect not only railway operating costs and returns, but also railway investment for modernization, etc. Again, the events of the depression, with the growth of nationalism, have affected armament costs in many countries, and this may react on the future level of Canadian expenditure on national defence.

Given the fact that future export booms are likely to prove spasmodic, maintenance or partial stabilization of the Canadian national income would necessitate some expansion of

activity for the home rather than the foreign market in order to insulate the Canadian national income from the full effects of external disturbances. If, because of unco-ordinated policies of the different governments (i.e. competition in services, in provision of public investments, or in search for revenues), or because of lack of business confidence, no expansion of home investment is possible, except, as in the past, on the basis of an export boom, the future fluctuations in national income are likely to be considerable, with depressions involving shifts of financial responsibilities from exposed areas or persons to the federal government. The fact that consumption was maintained in the recent depression by government relief, and works financed by credit and borrowing, and by the spending of the savings of individual households and firms, suggests that future resort to such sources may be increasingly difficult. Aggregate government policies, with respect both to the ends of expenditures, and to the various methods of financing these (particular taxes, credit and borrowing) are closely connected with the state of business confidence, the incentives to invest, and the undertaking of new ventures.

SUMMARY

(1) Since the War the Dominion financial position has been dominated by uncontrollable expenditures, and by the tendency of its revenues to depend considerably on customs duties and of its expenditures to increase in depression by reason of railway deficits and other special items.

(2) The years following 1929 reinforced these tendencies. The fall in customs revenues was so great as to necessitate considerable widening and deepening of the revenue structure. The rise in special "depression" expenditures - drought relief, assistance to certain provinces and industries, and the railway deficits - was considerable, and their level proved comparatively constant during the years up to 1936. By

1936 ordinary expenditures were back to their 1930 level, so that total current expenditure was still well in excess of revenue, despite the tax changes and the fair degree of economic recovery in 1936. The current deficit was $75 million.

(3) The size of the current deficit from 1930 onwards - it averaged almost $120 million a year in the 1930-6 period - was sufficient to induce a great contraction in Dominion capital expenditures. They had been at a peak of $190 million in 1929, but had been cut to $9.4 million in 1934. They were $5.6 million in 1936.

(4) The finance characteristics of the Dominion in this period may be contrasted with those of the provinces, by showing their total deficit (including capital expenditures) for the years 1930 to 1936 inclusive.

	1930-6 (inclusive)	
	Dominion	All Provinces
	$ Millions	
Current Deficit	829.5	290.3
Capital Expenditures	203.3	358.4
Over-all Deficit	1,032.8	648.7

The special depression expenditures that lay on the Dominion served to push it further than the provinces from a position of balanced budgets. And the Dominion's concern with its current deficit compelled it to reduce its capital expenditures quite far below those of the provinces. In the boom years (1925-9), the Dominion's capital expenditures ($340 million) had exceeded those of the provinces, ($212 million). But of the Dominion and provincial capital expenditures from 1930 onwards, the Dominion's share was only 35%.

(5) Of the debt increase between 1930 and 1936, in both the Dominion and the provinces, the Dominion's share was 68%. The Dominion's outstanding debt rose from $3.8 billion in 1930 to $4.8 billion in 1936. According to the balance sheet, this debt increase of one billion dollars went largely to railway advances (over $358 million), relief (over $345 million), to special loans to provinces for relief, to the farm loan board,

and to other active assets (over $164 million). Harbours and works received less than $80 million between them.

(6) Despite the debt increase, the Dominion's annual net debt charges have been held down, principally by conversion operations. Treasury bills have been cheap, but only a tiny proportion of the debt is represented by this form: their importance has been in their value as market manipulators. The Dominion's debt charges (less interest received) formed about 35% of net expenditure in 1936, as against 20.0% for the provinces as a whole.

(7) In the revenue system, all taxes except customs and excise were in 1936 above their 1930 level. Of the taxes, the 8% sales tax was the biggest revenue producer yielding almost 30% ($112.8 million), with customs duties yielding 22%, the corporation income tax 15%, the excise duties 12%, the personal income tax 11%, and the manufacturers, importations, stamps, etc., 10%. In view of the fact that the customs duties were still $100 million below their 1928 level, any recovery of national income to the level of the late twenties would probably considerably increase the yield of these duties, as well as the yield of the income and sales tax. It is unlikely, however, that the national income in 1938 will exceed that of 1937. A recovery of national income to the boom levels, or even beyond the 1937 level (which was only midway between the previous depression and boom extremes) is not immediately in sight. (August 1938).

(8) The expenditure system is not likely to alter considerably in the immediate future. Declines in the special "depression" expenditures, which might be hoped for in the event of greater economic recovery, are likely to be counterbalanced by some expansion in capital and other expenditures which were reduced in the depression (1930-3) and have not yet been fully restored. Furthermore, the level of defence expenditures, transport expenditures, and perhaps welfare expenditures, may be influenced for some time by forces tending to raise them.

Financial Position of Prince Edward Island

According to the measures of debt and taxation commonly used for comparing the financial positions of governments, Prince Edward Island's statistical standing appears favourable. Her provincial (plus municipal) debt per head is only about one-third that of the provinces as a whole. Her taxation per head is about one-quarter of the general average. In relation to the net value of production, taxes and debts appear to be less onerous than in most provinces.(1)

While the statistical and accounting position of the government is not unfavourable when compared with that of many other Canadian governmental units, some care must be exercised in applying these measures to Prince Edward Island's situation, and deductions made from such comparisons must take into consideration the special circumstances that dominate the Island's economy.

The geography of the Province (i.e. its position with respect to the other parts of Canada, its smallness of size, and its suitability only for agriculture and associated pursuits, including fishing) resulted in a group of conditions that were unique in the federation. The Island's lack of a public domain was another distinctive characteristic. These factors underlay the discussions that preceded the entrance of the Province into Confederation, and the financial relations then established with the Dominion, combined with the conditions imposed by geography and history, have dominated the provincial expenditure and tax system since that time. These circumstances suggest that a review of Prince Edward Island's financial position ought to be mainly concerned with its special features, and less

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(1) The debt charges (less interest received) took only 17% of the Island's net expenditures in 1936, as against 21% for the provinces as a whole, and as against 28% in Nova Scotia and 40% in New Brunswick.

with comparisons between it and other provinces. Its financial history is very much the history of its relations with the Dominion government.

The Island's position, its almost complete isolation in winter, and its need for subsidized transport, were compelling considerations in Prince Edward Island's entry into Confederation, although at the time (1873), the need of credit to finance the railway (begun in 1871), and of funds to buy out the remainder of the absentee landlords, were influential in shifting provincial opinion towards Confederation. But the economic need for continuous communication was permanent and urgent, and the alleged non-fulfilment of the Dominion's promise to maintain continuous communication was a major issue from Confederation onwards. From Confederation on, the provision of transport was out of the Province's hands, the Dominion taking over the P. E. I. railway in 1873, and accepting responsibility for communication with the mainland. Thus, if the Province desired to improve its communications in order to expedite economic development, it had to proceed, not by giving provincial subsidies or bond guarantees to transport concerns, as most provinces did, but rather by pushing its "transportation" claims at Ottawa. The frequency of its claims for better communication, and for damages for delay in provision of communication, was thus the measure of the Province's estimate of its transport needs. The fact that communication was a Dominion responsibility was important in relieving the Province of new commitments with respect to transport, and was one reason for a small debt growth in the Province.

Another reason was the size of the Province. The need for communications (telephone, road, etc.) in the Island was small compared to the need in other provinces where such equipment had to be laid down to encourage settlement. In Prince Edward Island, as in the older sections of some other provinces, the provision of such equipment tended to follow

rather than precede settlement. In newer western areas where, especially during the pre-war boom such equipment was often provided in order to hasten settlement, the government investment might later prove to have been in error if settlement did not proceed according to expectation. This factor adding to debt burdens was absent in Prince Edward Island. Again, the Island did not face the communication problem of pulling together widely separated areas, or connecting settlements across regions where roads were expensive because of the need for grading, levelling, and bridging. In short, the size and the nature of the Island's terrain tended to keep down the per capita costs of roads and other communicative equipment. In addition, the smallness of the area relieved the government of costs of co-ordination, which tend to increase rapidly as the size of a territory increases.

The smallness of the area was not however an unmixed advantage in public finance. Some costs (legislation, justice, and to some extent, administration) are in the nature of overhead costs, and the minimum possible size of this framework of government may be larger than that required by a small community. It is noteworthy that in 1871 Prince Edward Island's expenditures per head were higher than those of other provinces, but as the population increased to 1891 and little change in the technique of government was necessary, government expenditures per head fell, and thereafter remained almost unchanged until the post-war period saw the addition of new services. Since this addition of new government services, the percentage of Prince Edward Island's revenue that is spent on general government, administration of justice and legislation has risen and in 1936 amounted to over 13% of the revenue as against 8% in Nova Scotia, and this despite lower average salaries on the Island. In short, while smallness of area has limited capital expenditures, not only absolutely but relatively, it has tended to make certain costs of government comparatively high despite

"frugality".

The agricultural nature of the Province limited the need for municipal government, and the provincial government undertook to administer certain services usually entrusted to municipalities, particularly education. Moreover, certain local services given in larger municipal areas elsewhere were given only modestly in Prince Edward Island. The requirements and the costs associated with urbanization on the Island were small. Thus if it is shown that provincial expenditures per head were approximately equal in Prince Edward Island, Nova Scotia, New Brunswick, Ontario and Quebec, at the beginning of the War, this meant that the total government (provincial and municipal) expenditures per head were probably smaller in the Island than in the other provinces mentioned.

These circumstances of geography, size, and industry have combined to dominate the fiscal history of the Province. Its lack of diversity in resources and of a frontier, prevented errors of optimism about expansion. The smallness of its area and Dominion responsibility for transport also prevented debt growth, so that Prince Edward Island entered the post-war period with a small debt, just over $1 million. In December 1921, the total outstanding debt was represented by:

Assets.	$000
Investments	4.5
Public Works	1,234.2
Other Expenditures	1.4
Current Deficit	232.8
	1,472.9
Less Sinking Fund Reserve	232.8
	1,240.1

Before the War, the Dominion subsidy formed a very large proportion of total provincial revenues: in 1913 it was 71%. Up till then, therefore, total revenues were comparatively insensitive to local conditions, and to agricultural

fluctuations in particular: revenues expanded mainly in step with the subsidies. Of the total revenue, 20% came from provincial taxes which did respond to agricultural variations. Since there was little diversification in industry, and no public domain, the Province did not enjoy many increments of wealth. Regional income was dependent mainly on agriculture. Consequently there could be no great dependence on corporation taxes, succession duties, or domain revenues. Of the taxes raised by the Province, the general land taxes were the most important (although in 1913, the boom in the fox industry yielded special fox tax revenues). There was an income tax on persons, and at this time it produced as much revenue as the corporation taxes, which lay mainly on banks (deposits and loans) and on fire insurance companies (flat rate). In 1913 the revenues were as follows:

1913 Revenues

	$000
Subsidy	382.2
Taxes	105.2
Others	48.5
Total	535.9

In the expenditure system, education was the outstanding item, taking 33% of the total: government, legislation and justice combined took 22%, highways 21%, welfare 11%, debt charges (ex sinking funds) 8%, and agriculture 4%.

While the Province lacked opportunities for large increments of wealth, and so for extensions of its tax system, there was some compensation in the stability and gradual expansion of the Dominion subsidy.

Prince Edward Island's unique financial position in the federation in the pre-war period is perhaps indicated by the fact that its expenditures, even up to 1916, were still less than 30% above the 1873 level. Up to the War, the financial history of the Province had been mainly an attempt to keep

expenditures in line with revenues that depended greatly on the level of the federal subsidy. During the War, however, and in the post-war period, Prince Edward Island was affected by the new trend of expenditure growth that was common to all provinces, and this indicated that revenue possibilities would have to be further explored. Since then the proportion of total revenue raised within the Province has increased. Subsidy readjustments, like those following the Duncan and White Commissions, have been upward but the steady increase in total revenues and their annual variations are attributable largely to the Province's own taxing efforts. Between 1913 amd 1921, current expenditures rose by over 50%, welfare and education showing the most pronounced growth. By 1921 these two items accounted for half the total expenditures. Debt rose from $962,000 to $1,240,000, partly as a result of increased current deficits, but mainly because of new public works, the investment in which increased by 29% between 1913 and 1921. In these conditions additional revenues were necessary, and as a result of the expansion of the revenues raised within the Province, the subsidy, which in 1913 had yielded 71% of revenue, by 1921 yielded only 48%. Property and income taxes, which together had given 8% of revenue in 1913, yielded 21% by 1921. Corporation taxes provided 4% of total revenue in 1921 as against 3% in 1913. Amusement taxes were added but were not important. Liquor control and automobile licences, which yielded small sums in 1913, together formed 11% of total revenue in 1921. The revenues in the two years were as follows:

	1913	1921	Increase
	$000		
Subsidy	382.2	382.2	-
Taxes	105.2	303.9	198.7
Licences	19.1	56.3	37.2
Liquor Control	1.4	49.5	48.1
Others	28.0	4.6	-23.4
Total	535.9	796.5	260.6

Revenues, buoyed up by the post-war boom, declined with the 30% reduction in the net value of production that occurred in the post-war depression. The increased use of the motor vehicle did give new returns from gasoline taxes and automobile licences, but these were still not important revenue producers in 1925, yielding only over 10% of the revenues. The yield from general land taxes tended to contract, and there was a considerable fall in the returns from miscellaneous taxes, partly due to the repeal of the poll tax in 1923.

Although revenues fell in the depression of 1921, expenditures proved intractable, and indeed tended to rise as a result of new expenditures on highways, agriculture, and education grants. The resultant deficits induced the Province to widen part of its tax system, by the introduction of gasoline taxes, by some changes in corporation taxes, the most productive of which was the flat rate tax on railway companies. The yield from income taxes on persons (including the tax on personal property) was also stepped up. By 1926, the federal subsidy was yielding 43% of the revenue, the new gasoline taxes 4%, the enlarged corporation and income taxes 13% and 8% respectively. Tax revenues had increased by 12% over the 1921 level, mainly by readjustment of the tax system. By 1926 also liquor profits and automobile licences were beginning to prove more buoyant, and a surplus emerged on ordinary accounts. Between 1921 and 1925, outstanding debt had increased by $859,000, accounted for mainly by current deficits. The surplus in 1926 was great enough to permit a slight reduction in debt (by $18,000).

In 1927 a deficit emerged again. The additional subsidy recommended by the Duncan Commission was paid first in that year, and involved an extra $125,000. But revenue rose by only $20,000, the new subsidy being almost offset by tax reductions (land taxes fell by $22,000 between 1926 and

1927, and income tax fell by $16,500), and by a fall in liquor revenues. The effect of the increase in subsidy, and of the fall in taxes, was to make the Dominion subsidy again the outstanding revenue producer. In 1926 the subsidy had yielded 43% of revenue and taxes 39%, but in 1927 the subsidy provided 56% of the total revenue, and taxes only 29%. In 1928 taxes increased their yield again, and contributed 36% of the revenue, but land taxes still were 11% below their 1926 level. In 1928 also a road tax was added, and gasoline and income taxes were up slightly. The road tax was imposed as a result of the new level of highway expenditures, there being a 48% rise in highway costs between 1926 and 1927. Highways continued to absorb a larger share of the expenditure until by 1931 they took 34% of the total.

Up till 1931 welfare and debt charges increased no faster than total expenditures, while education, which had formed the major provincial expenditure up until 1925 (when it was 35% of total), had expanded only a little, and by 1931 was only 23% of the total. The highway costs were beginning to dominate the current expenditures of the government, and the other expenditures, particularly those on welfare and education (which together had formed 49% of the total in 1925) were being checked, although demands for their enlargement were fairly insistent. The highway programme was adding slightly to debt also, and therefore affecting the level of debt charges.

From 1928 to 1930, there was a surplus on current account, but the annual capital expenditure on highways increased annually, necessitating additions to debt each year, additions that were small absolutely (averaging only $197,000 in each year) but important in relation to the Island's previous debt history. However, by 1930, the Province's outstanding debt was $2.8 million only, represented in its balance sheet as follows:

Assets

$000

Debenture Discount unamortized		12.7
Advances		36.5
Buildings		40.3
Roads		942.6
Other Public Works		1,447.2
Other capitalized expenditures		15.6
Current Deficit		1,033.5
		3,528.4
Less Sinking Fund Reserve	568.2	
Capital Surplus	130.4	698.6
Total Outstanding debt		2,829.8

By 1930 the economic position of the Island revealed the difficulties arising from almost complete dependence on agriculture. As the Province had a fairly well balanced agricultural economy, the depression did not produce widespread destitution, but the loss of potato markets, the great fall in potato prices, and the contraction of the dairy product markets in the Maritimes reduced cash income and contracted provincial revenues. The subsidy, however, was a stabilizer which prevented total revenues from falling to the same extent as the land taxes or income taxes. Land taxes fell by 37% between 1929 and 1932, and income taxes by 25%: between 1930 and 1933 motor licences fell by 55%. But revenues as a whole remained stable until 1931, after which they rose, mainly by increased yields from corporation taxes (from the new tax on the capital stock of miscellaneous companies), from gasoline taxes, and from the road tax.

Expenditures rose in 1931, mainly on projects begun earlier (principally in highways, but also in welfare and in education), and a large deficit resulted in that year. The deficit was $232,000, the capital expenditures $282,000, and after other adjustments, debt rose by $547,000 in that year. Capital expenditures on highways had fallen by $100,000 below the 1930 peak ($239,000), but relief works absorbed $113,000.

Expenditures were cut in 1932, but by 1934 they were back at the 1931 level, and after a rise in 1935, were in 1936 again near the 1931 level. The distribution of expenditure had altered in the interim.

	Increases between 1931 and 1936		Decreases between 1931 and 1936
	$000		$000
Net Debt Charges	77.3		
Welfare	102.3		
Education	24.6		
Government	11.9		
Domain	1.7		
Other	5.3		
Highways			197.4
Justice			32.8
Legislation			10.1
Agriculture			7.3
Increase	223.1	Decrease	247.6

There was, therefore, a $24,500 decrease in expenditure between 1936 and 1931. Additional debt and welfare costs were offset mainly by a reduction in outlay for highway maintenance. Expenditures had been raised in 1935 by restoring outlay on highways, agriculture, justice, legislation to an earlier level, and by increases in government and education, but this so far raised the deficit in that year that cuts were again made in 1936, bringing total expenditure back to the level of 1934 and 1931. In short, the rise in the debt and welfare charges has caused competition among the other services for the remainder of the expenditure. This competition has occurred even within the welfare group as the costs of relief, charity and old age pensions have limited the amounts available for mental institutions, public health, hospital grants and other welfare services. Apart from relief costs, however, welfare increased from $158,000 in 1931 to $231,000 in 1936.

The fact that the budget was balanced in 1936, when revenues greatly exceeded previous levels by means of large expenditure cuts, especially on highways, suggests that

expenditure needs are likely to prove strong in the near future. That the low level of highway charges will be difficult to maintain is evident from the increased allocations in the 1937 accounts. It is likely also that certain welfare expenses will increase, especially those that are still below their previous levels.

As a result of the new and growing expenditure needs, the accumulated current deficit increased by $361,000 during the years 1931 to 1936, inclusive, and this occurred despite a broadening of the revenue basis. The federal subsidy increased in 1935, following the recommendations of the White Commission. In 1934 it had yielded 41% of the revenue: it was increased so as, once again, to form approximately half the revenue. But by 1936 it was again nearer 40% than 50% of total revenues. The tax basis was also widened during the depression. After the large 1931 deficit, the corporation taxes were raised both in 1931 and 1932, and as a result these taxes doubled their yield between 1930 and 1936. The increase was due almost entirely, however, to the new tax on domiciled companies and not to any enlargement of the number of companies doing business in the Province. This new tax yielded $70,000 in 1936, and the other corporation taxes $91,000, only $9,000 above their 1930 level. The main increase in tax revenue came from the gasoline taxes, but these cannot be increased indefinitely, or even perhaps beyond the present high rate of 10 cents per gallon without appearing burdensome to tourists accustomed to cheaper gasoline. The land taxes have also increased, and the renewal of liquor control has added a small amount to the total revenue.

The debt of the Island is still low, and its sinking funds are very well maintained. Nevertheless its outstanding debt doubled between 1930 and 1936. The following table shows the yearly debt charges over this period:

	1930	1931	1932	1933	1934	1935	1936
			$000				
Current Surplus(+) or Deficit (-)	+39.9	-231.9	+17.7	+9.5	-111.0	-209.7	+164.2
Capital Expenditures							
Buildings	29.3	10.3	79.1	227.4	80.1	48.4	49.7
Roads	239.4	139.9	74.8	50.8	64.1	95.0	54.6
Relief Works	-	112.6	114.0	-	98.2	563.1	217.6
Other	8.7	19.4	4.9	5.6	7.6	25.0	41.2
Total Capital Account	277.4	282.2	272.8	283.8	250.0	731.5	363.1
Overall Deficit	237.5	514.1	255.1	274.3	361.0	941.2	198.9
Debt Increase	221.1	547.4	289.1	278.2	357.9	1,054.2	214.7

Capital expenditures remained fairly steady up to 1935, although the various items changed in 1930-4. Road work tapered off to 1934, but relief works, mainly on highways, tended to offset the decline in highway expenditures. In 1933 public building expenditure reached a peak, the Province then having under construction a new hospital and school. In 1935 and 1936 capital expenditures were above the previous levels, primarily because of relief works. In 1935 also the rise in ordinary expenditures, already discussed, led to a considerable deficit, and thus added greatly to the debt increase in 1935. In 1936 ordinary expenditures were cut, revenues were up so that a surplus emerged, and the debt increase, though back to the 1930 level, was still considerably above the pre-depression average.

Outstanding debt rose from $2.8 million in 1930 to $5.6 million in 1936, an increase of $2.7 million, or nearly 100%.

SUMMARY

(1) The debt of the Island is still low, and the sinking funds are well maintained, so that its accounting position is good. But the recent rate of increase in debt has been high, in the light of the Province's history, and the forces that have made for this change may prove persistent for some time.

(2) Expenditure needs have tended to grow, partly because of the demand for social services and partly because of the economic position which has been affected by fundamental as well as short-period "depression" conditions. The contraction of the Cuba and U.S.A. potato markets, the cessation of emigration on the previous scale, and the increased intensity of competition in dairy products by the other Maritime Provinces have reduced the cash income in Prince Edward Island, and this decline affects the government's expenditure needs and revenue possibilities. The demand for welfare and educational services is unlikely to contract. The attempt to encourage the tourist trade to help to maintain cash income may also lead to a continuance of highway and other expenditures.

(3) Although subsidies still form over 40% of the revenues, the amount of revenue that has to be raised within the Province tends to increase. The possibilities here depend on returns from the trade in potatoes, and from the side lines of dairy and fox farming. Although the subsidy acts as a stabilizer on revenues, especially in depression years, the revenues cannot be said to be elastic. Furthermore, the budget now contains more uncontrollable items than in the pre-depression years, and this increased rigidity indicates that future expenditure needs will have to be met rather by increased revenues than by readjustments of expenditure or savings.

FINANCIAL POSITION OF NOVA SCOTIA

After Confederation there was for Nova Scotia, as for other Canadian governments, a short period of comparative financial smoothness. Certain functions had been transferred to the Dominion government, as had also been the debts of the Province, and the grant of better terms to Nova Scotia in 1869, with the additional debt allowance of 1873, gave the Province a reserve of spending power. Expenditures, however, advanced by 90% between 1869 and 1876. The main upthrust to the expenditure level came from the government's assistance to railway construction, and expenditures on roads. Since the municipalities did little road building, this cost fell heavily on the provincial government. Thus expenditures tended to run ahead of revenues, and the reserve of spending power dwindled. At this time the revenue system of the Province was fairly narrowly circumscribed, for two reasons. On the one side, the electorate was strongly averse to direct taxation, so that the Province had to rely largely on the federal subsidy and on its territorial revenue. On the other side, the people of the Maritimes were suffering rather more than people elsewhere in Canada from the changing technique of industry, especially in shipping. The economy of the Province had to adjust itself not only to new national policies adopted within Canada, but to a world-wide change in industrial techniques.

Attempts were made to secure further subsidy readjustments, and when these failed the Province resorted to borrowing. Only one direct tax was applied in this period - succession duties in 1892, and it proved a minor source of revenue for some time.

The revival in world trade after 1896 gave temporary relief to the provincial government. The formation of the

Dominion Coal Company, and the expansion of the coal trade in Canada's great development up to 1912, led to buoyant revenues from coal royalties. By the time of the general subsidy revision in 1907, mining royalties provided about half the total provincial revenues, and the subsidy about 30%. In these conditions of growth, the fiscal system needed little alteration, and the increased subsidy of 1907 made possible certain additional expenditures, especially on technical education. It seems also to have played a part in inducing demands at this time for old age pensions.

From 1896 to 1910 there was no financial strain. In Nova Scotia, as elsewhere, the period was one of development and optimism. The provincial government encouraged a small railway boom, spending over $5 million between 1896 and 1912 on 400 miles of road, and securing $2 million from the Dominion for the same end, while the Dominion government also assisted in dock and harbour building. This coincided with and encouraged the investment of private capital, particularly in iron and steel, but also in wool, ships, fisheries, tanning etc. In the light of later experience, this appears as a period of boom conditions, especially in Halifax and Sydney. Yet the nature of the urban construction boom served to emphasize economic difficulties in the rural areas. Agriculture was lagging noticeably in development, and was unable to withstand the competition of other provinces in wheat, grains, meats, certain fruits, and certain dairy products, particularly butter, eggs, and poultry. Special government assistance was necessary, as it was also in New Brunswick, to encourage land settlement and promote the raising of products in which external competition would be less severe. Despite this encouragement, the rural areas remained fundamentally weak in all but a few districts suited for specialization in certain products (apples,

dairy, etc.) At the same time there was evidence that the timber resources in certain localities were being worn out as compared with the resources in some regions, particularly British Columbia, that were about to compete in the overseas markets.

The economic difficulties facing the rural areas led to new demands for roads to round out these areas, and link them to the more quickly growing urban centres. The Province had already spent money on railways to this end (1906-1912): the same objective was sought in the new road programme of 1911; in 1914 a commission was established to consider the possibilities of hydro-electric power development, and it was to be concerned at a later date with improving the amenities of the rural life. But by 1911 the government, which had been spending half its revenues on debt charges, education, and hospitals, found it necessary to enlarge its public works programme for road purposes. At the same time, the demand for further hospital accommodation was becoming acute, and in 1912 additions to special departments were made.

Despite the optimism of the period, (and partly because of it), the government had to improve its revenue position in 1912 by the adoption of certain corporation taxes, by motor vehicle taxes, and by attempts to apportion to municipalities certain costs of reconstructing bridges, etc. The constantly growing costs of debt, of education, hospitals, and roads, necessitated the change.

By 1913, the outstanding debt was $11.7 million, represented in the balance sheet as follows:

	Assets (Thousands of $)
Taxes Receivable, etc.	282
Halifax & S.W.Railway	4,447
Roads and Buildings	5,893
Advances	4
Current Deficit	1,381
	12,007
Less Sinking Fund Reserve	326
	11,681

At this time, the revenues depended greatly on the domain and the subsidy, the former yielding half the total, and the subsidy 38%. Taxes provided only 8%. The main expenditure then was on debt, (19% of the total) with education taking 24%, and roads 20%. The expenditures already indicated the special circumstances that affected the economy. Road expenditures seemed likely to increase considerably, and debt charges, which were due largely to developmental projects, were already taking a not inconsiderable part of the total expenditure. By 1913, some of the inherent difficulties in the Province's economy were reflected in the financial position. Expenditure needs were increasing for communication equipment, for agricultural aid (training, demonstration work, clubs), for assistance to the railway serving these areas. And since the revenue depended largely on returns from the natural resources, the yield began to decline as a result of the collapse of the boom. Halifax alone continued its boom right into the war period, and that was partly because of the federal programme of constructing docks and railway terminals. If existing expenditures were to be maintained, and still more if new developmental ones were undertaken, some broadening of the revenue basis was desirable.

In these conditions, the position of the Province within the federation began to receive increased attention. Complaints about the financial arrangements had not been absent in the past, but the passing of time was clarifying the Province's position. Before the War, there was concern about the political status of the Province within the federation and its loss of members in the federal house. Its territorial status also became an issue. It began to be increasingly clear that the increments in capital values (both industrial and agricultural) accruing to other provinces were very largely the result of "frontier" development (wheat,minerals) and that the readjustment

of frontiers for all provinces except the Maritimes greatly affected their relative chance of obtaining capital increments. This position was clearly stated by Premier Murray in 1913 in a letter to the federal Prime Minister. A third issue in federal-provincial relations did not become crystallized until the post-war period; it concerned the economic status of the Province. The full implications of Nova Scotia's lag in development were not appreciated until after the immediate post-war depression. In all provinces except the Maritimes, the immediate post-war depression (1921) was comparatively short-lived, and in the Maritimes it became obvious by 1925 that deeply-seated influences were affecting the situation. When the issue of economic inequality was crystallized, the ground was laid for the Maritime rights movement, and for the ensuing Royal Commission (Duncan Commission). The lag in Maritime economic development, apparent in some sectors of the provincial economy before the War, was generally hidden during the war-time boom, which brought lucrative prices to farmers, especially to the fairly large group of farmers with wood-lots, and with timber to sell to the English market. The war boom served also to maintain the output of some urban centres, and to give opportunities for manufacturers for war purposes. The break of this boom in the post-war period, and the difficulties of recovery, revealed some inherent economic disabilities in the provincial economy. To some extent, the post-war economic position of Nova Scotia (and in New Brunswick) was more like that of the United Kingdom than that of the other Canadian provinces. The post-war period was one of slow adjustment to a new situation that did not encourage optimisn, and this condition left its imprint on the public finance system of the Province.

During the war period, the Province had to extend the basis of its tax system, but not importantly until 1919. It was in that year also that a new rate of increase in debt began

and that rate has continued steeply upward until the present, with a slight fall in the rate of increase from 1926 to 1928. The beginning of this debt movement is traceable to the extension of highways, in co-operation with the Dominion government, and to hydro-electric development. Alongside this were the new demands, common to all provinces, for improved education and hospital services, for better housing, and for the assistance of returned soldiers. As a result, corporation taxes were increased, succession duties altered, and increases made in motor licences and fees. In 1913, the combined taxes and licences had provided only 10% of the provincial revenue, but by 1921 they formed 56% while subsidies and domain, which together had accounted for 89% of the revenue in 1913, by 1921 yielded only 41%. This new revenue basis altered little until 1926, taxation tending to become more significant and the domain and the subsidy less so. But between 1921 and 1926 ordinary expenditures increased by almost one-third. Expenditures rose by over a quarter of a million dollars per year, and the bonded debt by about three million dollars a year.

Since Nova Scotia had no income tax as in some provinces, and no assessable property tax as in some others, and since its provincial government assumed functions that sometimes lay on municipalities elsewhere, certain services were bound to be on a smaller scale in Nova Scotia than in other provinces. Furthermore, the slowing down of economic progress after the War and the lack of buoyancy in public revenues, affected not only the total amount of the revenue available but also the direction of its distribution. Up to 1925, new expenditures were largely directed at public works and roads. In 1921, debt and highways accounted for 47% of the current expenditures: and this proportion grew to 57% by 1926. The

debt had been doubled between 1913 and 1921, principally by an additional investment of $7.8 million in public works, and of $1.6 million in the new power commission. Between 1921 and 1926 the debt rose from $21.8 million to $38.6 million, another $10 million having gone to public works, and another $2.7 million to the power commission. Debt charges, less interest received, were rising fairly rapidly, from 18% of total expenditure in 1921 to 26% by 1926. And current expenditures on highways rose from 29% to 31% of the total expenditures. These two items, therefore, dominated the expenditure system.

But the revenue system did not prove readily expansive. Domain revenues in 1925 were only half their 1913 level (to some extent because of the coal strike in 1925) indicating that domain revenues were not buoyant. The tax basis, which had been broadened during the war years was still inadequate. Corporation taxes provided half the tax revenues, and the property taxes more than one-third. The remainder came from succession duties and amusement taxes. In 1926 the tax basis was broadened by the yield of the new gasoline tax. The lack of revenues, and the necessity for directing 71% of the available revenues into debt charges and highways, left comparatively small amounts for government, social services (including education), agriculture, and conservation of the domain. Accordingly, there was little additional expenditure on education and welfare during this period. In 1921 only 28% of Nova Scotia's expenditures were on these services, while the provinces as a whole spent 36%: and up to 1926, Nova Scotia did not add much to these services so that by the latter year, only 21% of expenditure went to education and welfare. Accordingly it is accurate to say that expenditures on social services were lagging considerably behind the growth of such services

elsewhere in Canada, a circumstance that drew forth the sympathy of the Inter-Provincial Conference in 1926, and evoked special consideration from the Duncan Commission (p.19 report). The interim payments recommended by this Commission were intended to allow the Province to undertake, among other things, a more extensive programme of such services.

The post-war financial history of Nova Scotia (and New Brunswick) is important in revealing the first notable example in Canada of regional economic retardation that was sufficiently persistent and widespread to indicate the need for remedial action. The retardation reduced the revenue possibilities of the provincial government, and at the same time increased its expenditure requirements. The circumstances called for capital expenditures that would increase investment in the region, and implied also that social needs would tend to be greater than in a region enjoying a rapid increase in wealth. But retardation rendered such government expenditure policies difficult.

Economic conditions did little to increase the taxable capacity within the area. The Province could either apply current revenue (and new borrowings) to what seemed to be productive expenditures, or could concentrate on social and other services that would mitigate the effects of the economic position. Up to 1926, Nova Scotia relied mainly on the former policy, and extended public works, and the power undertaking. But this policy left less than half the revenues available for government, welfare, etc., and anyway the government investment was not sufficient to offset the factors causing retardation. In so far as the Maritime economic position was due to lack of resources comparable to those of other regions in Canada, or to the loss of ability through emigration of many enterprising persons, or to lack of a national economic policy designed to profit this area as a whole, the developmental expenditures of the Province

could hardly offset the direct and indirect effects of all these factors. These factors had operated for some time, and their effects had sunk into the economy. To that extent, their influence was strong, and the investment expenditures of the Province did not counterbalance them. The government investment helped to maintain households and firms, but created no spectacular increase in private investment in the region. And at the same time, the level of debts and of public works expenditures left little revenue available for other services. But other provinces, not affected by underlying difficulties that severely curtailed their revenue possibilities, were improving their standard of social services, and the Nova Scotia government was therefore confronted with a popular demand for services on standards comparable to those maintained by other provinces. In view of the economic difficulties, especially in certain districts, the need for government social services, free or at less than cost, seemed to be greater in the Maritimes than in areas of Canada where income levels were higher.

Welfare expenditures lagged up to 1927 in Nova Scotia, as did also expenditures on education and agriculture, but thereafter the broadening of the tax base by the introduction of gasoline taxes, the increased Dominion subsidy, extension of Dominion help in transport rates, public works, coal movements, port development, and the renewal of optimism that followed these undertakings enabled the provincial government to give increased attention to social and other services. It established a training school for defective children in 1927, it considered again the possibility of paying old age pensions, it increased teachers' salaries, gave credit to farmers on long time mortgages, granted mothers' allowances, and made larger grants for hospitals and nursing, etc. In short, the history of the 1926-36 period is largely the history of the attempt to raise the standard of social services to levels comparable with

those elsewhere in Canada. This did not involve any reduction in development expenditures. They still continued to expand, even more rapidly than before. The consequence was that the increase in debt was much faster between 1926 and 1936 than in 1916-26, despite the widening of the revenue base. Between 1926 and 1936, outstanding debt increased by almost $46 million.(1) As a proportion of this total, the direct relief payments involved by the depression were comparatively small, amounting to over $2 million. But in addition to this, the Province provided relief work on roads, which, according to the balance sheet amounted to $5.2 million, and relief work grants to municipalities of $0.5 million. In all, however, the relief costs did not form a large proportion of the debt growth. Direct relief payments declined after 1933, although not with any rapidity until 1936 when the new government highway programme was well advanced, and general economic recovery was more pronounced. In short, relief costs proved fairly intractable until the Province had established a new level of government investment, a level that will remain until the hard-surfacing of highways is completed (i.e. at least until the end of 1938). The fixity of relief costs until 1936 is not unconnected with the fact that after 1930 opportunities for emigration to the U.S.A. and central Canada were reduced and the working population grew beyond what appears to have been the normal absorptive capacity of the Province. Government investment in highways since 1934 has helped to take care of this problem, just as it helped to lower the maintenance costs of roads charged to current expenditures, but after completion of the highway programme further works may be needed to create employment, just as there will be a need for high maintenance costs on highways as the new roads suffer wear. In other words, the low level of direct

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(1) From $38.6 million in 1926 to $84.5 million in 1936.

relief costs in 1936[2] was due, in large measure, to the government investment policy, as was also the level of current maintenance costs on roads. The level of total current expenditures of 1936 cannot therefore be taken as a measure of probable current expenditures in the near future, unless some new set of government capital expenditures follow on after the completion of the highway programme. In 1935 and 1936, the government investment in the new provincial building also served to maintain the construction industry.

In Nova Scotia the depression was met by the government by the provision of new equipment, as in highways, and by increased aids to industry, especially agriculture, fisheries, and mining. These aids are revealed in both capital and current account. They have taken the form of advances and loans (e.g. Land Settlement, Fishermen's Loans etc.) that have in all increased by $1.5 million since 1929, the government control of the Inverness Coal Mine, and more intensive work on agriculture out of current account. These expenditures for intensive development are still comparatively modest, but they appear to be a corollary to the expenditures on the extensive equipment like roads, rural electrification, etc. So long as the trend of labour and capital has been away, rather than to, the Province, intensive development may need to be fostered, partly to maintain the present economic position, but also to utilize the extensive equipment already provided. After completion of the road programme in the near future, this intensive development, already aimed at certain industries - the fisheries, agriculture, gold mining, etc. - may prove to be necessary on a somewhat wider scale, in order to secure a more balanced economy, and in order to offset the influence of certain long-time factors that create economic difficulty.

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(2) $95,000 as against $674,000 in 1933.

The expenditure system in Nova Scotia, which reflects its needs with respect to public works, and which was dominated by debt charges and highways works in 1926, still reveals these characteristics. By 1936, however, debt charges, less interest revenue, accounted for 28% of the expenditures, as against 26% in 1926: ih the interim, the proportion of ordinary expenditure absorbed by highways had diminished, as a result of the capital improvements on the roads. But even in 1936 net debt charges and highways absorbed 50% of the expenditure. The items that had grown in relative importance during this period were welfare and education, particularly welfare, which rose from 9% of expenditure, to 20%. In the provinces as a whole, welfare was by 1936 absorbing 35% of the total expenditure. The main upthrust to the welfare costs in Nova Scotia came with the introducing of mothers' allowances in 1931, and of old age pensions in 1934. By 1936 these two services formed over half the welfare expenditures. The remaining expenditures on welfare (health, institutions, hospitals, etc.,) are still at their 1928 level. It is likely that the health services will increase in the future. On no point was the Provincial Economic Commission (1934) more impressed than the need for extending medical services to areas unable to meet the costs of such facilities. Rural depopulation involved the breakdown of the system of medical attention (Report p.203), and so far, the Province had been unable to take any major steps to remedy this position. Any buoyancy of revenue would probably mean therefore a still greater expenditure to meet this obvious need. The preservation of at least some of the rural regions probably requires an increase in health services to implement the other maintenance expenditures (i.e. for the utilization of whatever opportunities for development may be created by highway improvement, rural electrification, aids to agriculture, fisheries, to general and technical education, etc.).

After welfare, education was the second growing expenditure in the 1926-36 period. In 1926 it absorbed 13%, and in 1936, 14% of the total expenditures, the actual education expenditure having risen from $636,000 to $1,210,000. Almost half of the increase went in aid to teachers, school grants and free school books making up most of the balance. Despite the aid to teachers, their salaries are still comparatively low. There are over 1,700 school units in the Province, each levying its own tax rate. Because of the needs of the backward areas and their small school units, there has been an inevitable growth in the proportion of provincial to total expenditure on education, but the need for still further outlay and reorganization is evident. While the grant for free school books gives relief to individuals, it does little to improve the system as a whole. The Province has still no vocational school.

The proportion of expenditure that goes to general government is lower than that of most provinces.(3) The same low proportion of expenditure on government is found in New Brunswick. To some extent, the difficulty of improving the standard of the civil service may be due to the "frugality" of the Maritime administrations. Civil service salaries were cut during the depression years.

The Provincial Economic Inquiry (1934), following on the investigation and recommendations on the civil service by Professor Dawson, placed at the "fore front of its recommendations" (p.87) the suggested reform of the civil service. So far as the future development of the provincial economy requires skilled investigation and supervision, the Province may find it necessary to increase expenditures on general government.

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(3) For general government, 6% in Nova Scotia as against 7% for the provinces as a whole. For general government, legislation and administration of justice, 8% for Nova Scotia as against 12% for the provinces as a whole.

Expenditures on public domain are small and have been kept fairly constant. Expenditures on agriculture have increased, but those on forests have fallen, perhaps below the minimum necessary in a region where conservation and protection are imperative. This item is likely to increase in the future.

Total expenditures on current account have risen from $5.0 million in 1926, to $8.8 million in 1936, and there are indications that the rate of growth is likely to be maintained for some time.

The revenue system in 1936 depended to a considerable extent on taxes, which yielded 45% of the total revenue. The federal subsidy produced 20%, licences 15%, liquor control 12% and the domain 8%. These proportions had changed somewhat over the last decade. The proportion contributed by the federal subsidy increased as a result of the Duncan and White Commissions' recommendations. Liquor control profits also increased.

In an economy where the level of the regional income tends to be low and the number of taxable subjects is not large, taxes have to be raised without adding much to the costs of enterprises, otherwise they may offset whatever beneficial effects emerge from the government's expenditure policy, and may even create further expenditure needs in the Province, for welfare, etc. This characteristic of regions suffering economic difficulty necessitates a careful adjustment of their revenue systems. Thus, while Nova Scotia has no income tax, it has high gasoline taxes, high licence fees for gasoline stations, comparatively high corporation taxes of certain sorts, and comparatively high succession duty rates. There is an attempt to secure the revenues in ways that will be least harmful to the local economy.

It is not surprising, therefore, that the revenue raised by the Province has depended more and more on gasoline and automobile taxes. In 1926 these together formed 18% of the revenue raised by the Province,[4] but in 1936, they formed 31%. It is to be noted, however, that the gas tax rates are now very high, and that it is undesirable to have too large a spread between the Nova Scotia and New England gasoline prices, lest tourists should begin to resent the high rates. The other notable increase in revenue raised came from liquor control, which yielded $50,000 in 1926, and $1,105,000 in 1936.

Over the period under review, the corporation taxes increased in amount, following the increased rates on banks, insurance companies, etc., in 1932, and the new taxes on chain stores and small companies, but these changes produced no marked increase in yield.

In 1926, corporation taxes produced $779,000 and in 1936 $1,118,000 due mainly to the increase in taxes on banks, insurance companies and miscellaneous companies' capital stock. Succession duties showed no marked change in the period.

With limited revenue possibilities and expanding expenditure needs, the Province did not find it easy to establish a favourable accounting position at any time during the period. On ordinary account deficits were more frequent than surpluses, and capital expenditures were fairly constant until raised in 1935, so that the overall deficit and the increase in outstanding debt was fairly constant until the depression. Between 1926 and 1930, the debt increase was due

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(4) In 1936, provincial revenues, after deducting the subsidy, were $7,579,000, of which $1,730,000 came from gasoline taxes and $1,249,000 from motor licences.

mainly to capital works. Debt rose by almost $17 million, $8 million of which went in advances to the power commission: the remainder went largely to public works, principally roads up to 1928, and in 1929 to mining development in the Inverness Mine.

Nova Scotia's capital expenditures, unlike those of other provinces, did not vary much in size between the boom and the depression years. In the three boom years (1927-9 inclusive) the capital expenditures amounted to $6.6 million: in the three depression years (1930-32 inclusive) they were slightly higher at $7.1 million. In the recovery years, they reached higher levels, and were $7.7 million for 1936 alone, the highway programme then being the outstanding work. The maintenance of capital expenditures in the depression, and their enlargement after 1934 probably were significant elements in the process of recovery, especially since the highway works touched most areas of the Province. The following table indicates the position after 1932.

	1933	1934	1935 (14 mos.)	1936
		(millions of $)		
Current deficit (-) or surplus (+)	-1.9	-1.7	-1.1	+ .7
Capital Expenditure	3.2	2.1	5.7	7.7
Over-all deficit	5.1	3.7	6.8	7.0

In 1933, the current deficit was at its peak. All revenue items (except the subsidy) reflected the depression conditions. The main declines between 1932 and 1933 in revenue were in taxes ($391,000) licences ($63,000), liquor ($303,000) and domain($99,000). The year of lowest revenue after 1929 coincided with the peak of direct relief payments, and a current deficit of $1.9 million resulted. Expenditures continued to rise a little, although 1936 expenditures were

very little above the 1934 level. In the interim, direct relief costs had fallen, but the introduction of old age pension payments in 1934 raised the welfare costs. Debt charges were up by 1936, and education had also risen. After 1933 revenues proved more buoyant. The revenues from gasoline tax and motor licences rose by $1 million, or nearly one-third of the total revenue increase. The increase in liquor profits, federal subsidy (White Commission recommendation) and domain revenues made up the remainder. As a result of the revenue increases, current deficits declined rapidly after 1934, and a surplus emerged in 1936. In 1935 and 1936, however, the capital expenditures rose to new levels for Nova Scotia. In 1934, public works had involved $1.6 million of government investment, but by 1936 the total was $7.4 million, ($6.5 million going to hard-surfacing of highways, and $0.7 million to the new government building in Halifax.) The increase in outstanding debt was $6.0 million in 1936. , In 1933, the debt increase was $6.8 million, but in that year the current deficit was an important contributor.

<u>Summary</u>

(1) Economic difficulty confronted certain parts of the Province in the pre-war period, but it was not until after the War, when other provinces were recovering from the post-war depression while Nova Scotia (and New Brunswick) were still experiencing some economic stagnation, that the special economic problems of the region were evident.

In Nova Scotia, the revenues were limited, and the expenditure system became increasingly dominated by debt charges and highway works, aimed at the development of the Province.

(2) The effect of the Duncan Commission recommendations was to remove some of the difficulties, and with improved revenues the Province was able to give increased attention to welfare and other services that were tending to lag in expansion as compared with other provinces.

(3) The depression from 1930-3 which impinged on an already comparatively weak situation, limited revenues further, and added to expenditure needs, particularly for direct relief.

(4) The increased government investment in the recovery period, coupled with small aids towards intensive development of certain industries, yielded a measure of economic improvement that helped to reduce direct relief costs, and to stimulate certain revenue, particularly gasoline taxes and automobile licences. The "White subsidy" also helped the improvement of revenues.

(5) Capital expenditures in the past few years have been directed largely at road building. As already indicated, this investment has probably gone far to aid recovery and to provide employment for the increased working population. It has probably also encouraged the growth of the tourist trade, and this in turn has affected the yields of the gasoline taxes in the past few years. The successful operation of a tourist industry probably requires more than the laying down of highways, and some additional government expenditures on the national park, and perhaps on equipment, and towards training in tourist service may prove necessary. The value of this industry to the government is not to be measured only by the direct returns received in gasoline or other revenues, but also by the provision of small cash incomes to households in rural districts. A successful tourist trade might not add greatly to revenues, but it would reduce the expenditure needs

of the government if it yielded cash incomes in rural or partially distressed areas. Road building may also encourage road transport and may ultimately affect transportation costs within Nova Scotia and between the Province and other regions, an end which would be just as important in reducing the future expenditure requirements of the Province as in raising its revenues.

(6) The revenue basis is still narrow and the recent sources of increase are unlikely to provide a steady uptrend into the future. Furthermore, the expenditure needs on welfare and education tend to be long-term. The needs are greater than in some other regions, the taxable sources are fewer. Lack of economic resiliency reduces the number of taxable subjects, and a cessation of government investment might again indicate the limited possibilities for expansion in the region. Even with the recent levels of government activity, there are still certain pockets of unemployment within the Province, and these areas have all the characteristics of so-called distressed areas.

The Financial Position of New Brunswick

New Brunswick in common with Nova Scotia encountered economic difficulty in the confederation period on account of the change in the technique of production, and the abrogation of the reciprocity treaty with the United States of America. The New Brunswick economy was based mainly on lumber, ship-building, and fishing. These industries met competition from steamships and railways, while cheap accessible supplies of timber within New Brunswick were becoming more scarce, and new supplies were being opened elsewhere. These conditions affected the fiscal position in two ways, restricting revenues within the Province, and necessitating new expenditures on roads and railways to promote development. Like Nova Scotia, but not to the same extent, New Brunswick enjoyed a period of some financial ease after 1873 (i.e. after the general increase in allowance at Ottawa, and the special allowance for lumber duties). New Brunswick, however, did not use up its Ottawa reserve so rapidly as did Nova Scotia. Nevertheless, at the end of the century, expenditures tended to outstrip revenues, and debt increased by the building of roads and railways. In the Maritimes the railroad problem was especially difficult, because water competition was keen, the railway facilities were idle for long periods in the year, and government assistance was pro tanto increased. In these conditions the Province had to extend its tax system in 1892, by the introduction of some corporation taxes and small succession duties, and at the same time pursued its claims against the federal government for arrears on the sale of the Eastern Railway Company (sold to the Dominion in 1884). Then, as after the Great War, the burden of uneconomic railways was a major issue in the New Brunswick economy.

At the turn of the century, New Brunswick was receiving 64% of its revenues from the Dominion grant, 23% from Crown lands and 11% from taxes (corporation, succession duties and liquor

licences).[1] On the expenditure side, education was the largest item, followed by public works, interest, and bridges. These accounted for almost two-thirds of the expenditure, the remainder being on government (justice, legislation, government and assembly), agriculture and health.

The improvement in world trade after the turn of the century led to increased lumber prices, and at the same time improved communications within New Brunswick gave access to some new timber sources, so that the revenue from the Crown lands increased greatly, and by 1911 formed 39% of the total revenues, almost as high a proportion as the Dominion subsidies.[2]

The period from the opening of the century to the beginning of the War was important in the financial history of New Brunswick. The government was inclined to pursue a double-headed economic policy that was not usual among Canadian provinces in the pre-war period, but has become more common in the depressed provinces in recent times. It was the policy of providing both extensive capital equipment (railways, roads, public works, etc.) and of providing also more intensively directed aids to certain industries to help them to increase their utilization of this extensive equipment. Before the War, the emphasis in most provinces was mainly on the provision of extensive equipment, and private enterprise invariably proceeded, in greater or less degree, to develop within that framework of transport, public works, and institutions. In New Brunswick, however, the spreading of capital equipment had to be implemented by aids directed at intensive development in certain industries and places. On the one side, since other Canadian governments were providing what seemed to be the basic conditions of expansion

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(1) In 1900 the total revenues were $758,988, of which the Federal Subsidy yielded $483,491, Public Domain $175,818, Succession duties $39,522, Corporation taxes $25,352 and Liquor licences $21,628.

(2) By 1911, total revenues were $1,347,077, of which the subsidy yielded $621,360 and the public domain $529,660, between them amounting to 85% of the revenue.

by the extension of transport facilities and public works, it appeared that if New Brunswick were properly equipped with such works, Saint John might become "the New York of Canada". The decision to undertake the Saint John-Quebec Railway (1912), so that Saint John would become the terminus of all transcontinental lines, was based on expectations of such developmental possibilities, and on the need to integrate the railway system begun before Confederation and extended by the construction of many short stretches of line. But on the other hand, the opening of the West, and the shift to dairy-farming in Ontario, were already creating competitive difficulty for New Brunswick agriculture, so that support had to be given in an intensive way to this industry. Encouragement was given to immigration, and attempts were made to improve the attractiveness of rural life (farms for settlers, improved roads, and an extension of the agricultural education programme after the Agriculture Aid Act of the Federal Government in 1913). At the same time, attention was given to the expansion of the potato trade with Cuba, to the development of gas and oil in Albert, and to the coal industry in Queen's. To further such intensive aid, new capital works were sometimes necessary (e.g. railway into Queen's and roads to farm areas).

As a result of this expenditure policy, and of the tardy development of manufactures, even as compared with Nova Scotia, the provincial revenues failed to keep pace with expenditures, despite new succession duties (1905), new taxes on banks and insurance companies, new taxes from the Highways Acts of different years, a change in Crown land policy with respect to timber and pulp licences, and a new tax on municipalities to assist the hospitals. The debt grew steadily from 1900, so that by 1913 the New Brunswick debt was about equal to that of Nova Scotia, while her economy was less diversified. General economic conditions served to encourage claims against Ottawa, claims for a share of the Halifax Award, claims for compensation for the liberal

subsidies given to the new provinces, claims for compensation for the extension of boundaries in Ontario and Quebec (that might contain "many Cobalts"), and general resentment at the loss of federal seats and at the implications of this loss. New Brunswick entered the war period with a debt burden that was gradually becoming heavy, especially in view of the fact that economic progress was not so rapid as in other regions in Canada. By 1913, the outstanding debt of the Province was $11.5 million., Of this total $4.1 million was indirect debt covering railway guarantees, the largest of which was the Saint John and Quebec Railway Company, that was later assumed by the Province (1917), $3.2 million had been directly incurred for highways and bridges, and $2.2 million for railway subsidies. The direct bonds amounted to $6 million and the treasury bills to just less than $1 million. The main source of revenue was still the subsidy, with public domain yielding the second item: between them they produced 81% of the total revenue. Taxes yielded 11%, succession duties being the main element. Current expenditures were as follows:-

	Expenditures 1913 $000
Highways, Bridges	356.8
Education	277.1
Debt charges (less interest received)	257.1
Government (including Justice and Legislation)	200.8
Public Welfare	99.8
Public Domain	75.8
Agriculture	58.5
Other	28.0
Total	1,353.9

At the outbreak of the War, then the province still depended mainly on the revenues that had been apportioned at Confederation, viz., the subsidy and the territorial revenue. Direct taxes were still insignificant. But the expenditure system was beginning to reflect the special needs of the Province, as well as the general trend of growth that affected education,

highways, etc. in all provinces. The debt charge in 1913 had grown to 19% of the expenditures, reflecting the extent of provincial developmental undertakings.

The War however served to reveal the factors that were dominating the economic, and therefore the financial, position of the Province. The War boom and high lumber prices encouraged that industry and this reflected itself in the domain revenues.(3) At the same time, the boom stimulated certain other revenues. The special tax on insurance premiums proved buoyant. New taxes on amusement and on wild lands, and new basic rates of succession duty, also served to raise the level of taxes from $159,000 in 1913 to $611,000 by 1921. The same boom stimulated the revenue from licences, particularly motor licences which rose from $11,100 to $274,400 by 1921. Revenues as a whole rose from $1.4 million in 1913 to $2.7 million in 1921. The new level of revenue permitted new government commitments, both on current and on capital account. As a result, by 1921 expenditures had grown by 151% over the 1913 level, as against 87% for all provinces, and outstanding in this growth was the new level of debt charges. In New Brunswick, as in other parts of the country, the rise in costs during the War had burdened the newly constructed railways, and railway liabilities which had been only indirect before the War, had tended to become direct. In New Brunswick, the Saint John and Quebec Railway Company was the main example: its bonds were assumed directly by the Province in 1917, and by 1921 the government investment in railways totalled $8.9 million, apart from the railway subsidies of $2.3 million. The other main capital expenditure during the War period was on highways. The Province had 11,000 bridges to maintain and renew, and a new road programme was begun to improve the highways for the growing motor traffic. Between 1913 and 1921, $8 million were spent on highways from capital account. Furthermore, the potentialities of hydro power were considered by a commission in 1918, and a power commission

(3) Domain revenues were $502,200 in 1913: $1,107,000 in 1921.

was established in 1920, with plans for developing power for Saint John. The government advanced $2 million for this in the first year, $1.6 having been spent by 1921.

As a result of these undertakings, a new level of debt charges emerged during the war period. The revenues however were buoyed up by the war boom, especially the domain revenues, but as a whole, the revenue basis was comparatively narrow, the subsidy and domain revenues still forming nearly two-thirds of the total. While the subsidy proved stable enough, there was no such assurance about the domain revenue, which depended largely on the lumber market, and on the state of the province's lumber resources in comparison with the resources of other areas at home and abroad. And the remainder of the revenue system from taxes and licences was limited by the buoyancy of the regional income. These tax revenues, as well as the domain revenues, had been pushed up by the war boom, and new commitments had been undertaken. If revenues failed to be sustained, the new level of debt charges would prove burdensome, and might lead to contraction of other current services. By 1921 net debt charges formed 31% of the total expenditures, as against 19% in the 1913 period. In addition, the new work on highways and bridges required increased maintenance charges, as did also the public domain, particularly for forest services and for fire ranging. Given these conditions, other services, like education and welfare, would have to be kept in check, unless revenues proved buoyant. A comparison of the 1913 and 1921 current expenditures (excluding sinking fund payments) follows:

	EXPENDITURE $000	
	1913	1921
Highways, Bridges, etc.	356.8	834.0
Education	277.1	442.2
Debt charges(less interest received)	257.1	1,057.7
Government (including Justice and Legislation)	200.8	471.7
Public Welfare	99.8	231.8
Public Domain	75.8	277.0
Agriculture	58.5	72.5
Other	28.0	6.8
Total	1,353.9	3,393.7

But forest production did not maintain its war-time values. Since 1920 there has been a steady decline, with some revival in 1924, and in 1928, and a deep depression in 1933. The revenue producing ability of the Crown lands has contracted,(4) not quite to the same extent as the net value of production, but since the costs of fire ranging tend to increase, the net surplus after deducting forest expenditures from forest revenues, fell by 57% between 1921 and 1936, and the net government returns in the depression years were less than 3% per annum of the value of forest production.

While forest revenues declined in the post-war period from their war boom levels, other revenues did not prove buoyant. The post-war depression affected not only the lumber trade, but also agriculture and shipping, and the regional income in New Brunswick, as in Nova Scotia, began to indicate the peculiar conditions that were affecting the Maritime economy. These conditions had been present in the pre-war period, but the general Canadian boom at that time promoted some economic progress, in the Maritimes, even if slower than elsewhere. The war boom again tended to hide the operation of adverse factors. In the post-war period, these factors became more apparent, and even when the Canadian economy as a whole began its recovery from the immediate post-war depression, the Maritime Provinces lagged in this recovery. Throughout the post-war years up to the time of the Duncan Commission, New Brunswick experienced growing expenditure needs, but no particular expansion of the revenue possibilities. In the post-war period the extent to which the government

(4)

	1913	1921	1928	1933	1936
		$000			
Forest Revenues	406.7	972.9	1,042.1	374.9	546.2
Wild Lands Tax	-	55.4	54.2	55.8	59.1
Total Revenue	406.7	1,028.3	1,096.3	430.7	605.3
Forest Expenditure	31.5	214.9	141.1	149.5	191.8
Forest "surplus"	375.2	813.4	955.2	281.2	413.5
Ratio of "surplus" to net value of forest production	-	3.5%	4.3%	2.9%	2.2%

has been affected by economic difficulties is indicated by its expenditure policy on capital works and on highways. In regions in which economic progress is being adequately pushed by private enterprise, governments need not expend so much on developmental projects. In New Brunswick, the pressure of economic retardation, and the attempt to provide works that would encourage enterprise (and tourist trade), have been perhaps the main concern of the government since the War. The extent to which the government has pushed these works is reflected in the fact that since 1921 net debt charges and highway expenditures on ordinary account have consistently absorbed at least 55% of the total expenditure. In the depression years after 1930, when most expenditures (except welfare) had to be pared down, and when highway expenditures on current account were also cut, the proportion still remained high because increases in net debt charges approximated the reductions in highway expenditure. The following table indicates the extent of these two services:

	1921	% of Total	1925	% of Total	1930 $000	% of Total	1933	% of Total	1937	% of Total
et debt harges	1,057.7	31	1,379.3	35	2,011.4	32	2,767.7	48	2,784.0	39
ighways tc.	834.0	25	986.5	25	1,894.0	30	700.2	12	1,154.1	16
otal urrent xpendi-ure	3,393.7	100	3,908.5	100	6,382.2	100	5,792.3	100	7,185.3	100

For the provinces as a whole, these two services in the post-war period absorbed less than one-third of the total current expenditures. The dominance of these two itmms in New Brunswick current expenditures limited the funds available for other services, especially as the lack of real revenue possibilities prevented a rise in revenues.

The capital expenditures which were giving rise to new debt levels, were mainly on highways, new electric power undertakings, and the Saint John and Quebec Railway.

The highway expenditures on capital account had grown with the emergence of motor traffic; and the provision of bridges in what has been called the "best-watered country in the world" tended to exceed that of highways until 1926.(5) Between 1921 and 1925 the expenditures on these items amounted to $5 million. The other capital expenditure that advanced was for government utilities, there being an increase of $3 million between 1921 and 1925. These two (highways and utilities) accounted for the increase in outstanding debt from $28.6 to $36.2 million. In utilities, $2 million of the $3 million spent went to the electric power commission, and $1 million to railways. By then, investment in railways had cost the Province over $9.5 million. Many other provinces had by then been relieved of their railway obligations by the Canadian National Railway, and provincial opinion in New Brunswick indicated that a similar transaction would be just in its case.

While the above capital expenditures were the important ones in adding to the provincial debt in the post-war period, small amounts were involved in certain other projects.

By 1925, the financial position revealed the difficulties with which the Province was faced. In that year there was a current deficit of over half a million dollars. The budgetary difficulties were fairly acute, despite the recent buoyancy of lumber revenues, the rapid rise in revenues from licences (particularly the automobile), and the rise in succession duty revenues from 1922. In his 1925 Budget Speech, the Provincial Secretary indicated that there would have to be increases in corporation (and amusement) taxes, and new taxes on gasoline and

(5) According to the provincial balance sheet, bridges accounted for $6.9 million in 1921, and highways for $4.2 million. By 1926 highways had advanced beyond bridges, accounting for $8.8 million as against $8.7 million for bridges. Since then, the highway expenditures advanced much more rapidly, especially after the inauguration of the hard-surfacing programme in 1934.

on real and personal property and income, based on municipal assessment. In view of the weakness of municipal administration, the inequality of assessment as between municipalities, the incompleteness of returns, the great discrepancies between the municipal assessment and the federal census returns on farm values, it did not appear as if the new income tax would be very equitable. It was not imposed, but other proposed changes were made. A gasoline tax of 3 cents per gallon was introduced, and there was an increase in certain of the corporation taxes, and in the amusement tax. An increase in tax revenues in 1926 resulted as may be seen in the following table:

	Revenues		
	1925	1926	Increase
		$000	
Corporation taxes	244	644	400
Gasoline Tax	-	118	118
Amusement taxes	49	54	5

The tax changes yielded $523,000 additional revenue. It happened also that succession duties increased in 1926, so that total taxes rose by $544,200 in that year, while revenues as a whole rose by $693,300, and a small surplus emerged on current account. In 1927, however, the Duncan Report was implemented by an additional federal grant of $600,000, and some of the new corporation taxes were remitted. They fell from $644,000 in 1926 to $413,000 in 1927, the fall in bank taxation and insurance premium taxes accounting for the bulk of the decline. This decline was of course more than offset by the increased federal subsidy, which had been equivalent to a 15% rise in revenues. Whereas the subsidy in 1926 had represented only 16% of the revenue, it rose to 24% in 1927. Despite the reduction in corporation taxes, revenues as a whole rose by more than the additional subsidy.

The implementing of the Duncan recommendations coincided with some improvement in New Brunswick trade, and a period of some optimism lasted till 1929. 1926 was a comparatively good year in production, and in addition the Duncan Commission had made special recommendations with respect to freight rate reductions, port development, and further inquiry into the Saint John - Quebec Railway situation. The boom that affected the whole Canadian economy occurred on a smaller scale in the Maritimes, and some buoyancy of revenues resulted. Public domain revenues rose by 19% between 1926 and 1928, but turned downwards again in 1929. Other revenues however continued to expand till 1930, and a surplus on ordinary account resulted in each year from 1926 to 1929. The main changes in the revenue position may be seen in the following table:

	1926	1930	Increase or decrease x
		$000	
Liquor Control	417.3	1,544.3	1,127.0
Federal Subsidy	666.8	1,266.8	600.0
Licences	622.5	965.8	343.3
Domain	1,045.9	880.0	165.9 x
Taxes	1,255.6	1,600.2	344.6
Miscellaneous	56.6	46.9	9.7 x
Total	4,064.7	6,304.0	2,239.3

About half of the increase in revenue came from liquor, a new form of liquor control having been established by 1928. One quarter of the increase was due to the "Duncan subsidy", and the remainder came principally from taxes and motor licences. The revenue system was still narrow however. The increase in liquor profits, which vary directly with public spending could not be regarded as permanent. The federal subsidy increase was due to a special investigation, and would prove stable. The motor licence increase was also likely to have fairly definite limits. Taxes increased by 27.4% but public domain revenues declined by 15.9%. Corporation taxes had fallen by the remission of taxation after the increased subsidy. But these declines had been

just more than offset by the increased yield of gasoline taxes ($528,000).(6) By 1930, taxation was yielding only 24% of the revenue.

The increased buoyancy of total revenues permitted again new expenditures on both current and capital account. The current expenditures rose as follows:

Expenditures

	1926	1930	Increase
	$000		
Highways	872.0	1,894.0	1,022.0
Net debt charges	1,510.5	2,011.4	500.9
Government (including Justice and Legislation)	467.0	729.6	262.6
Welfare	270.0	440.4	170.4
Domain	177.2	353.4	176.2
Education	539.9	693.2	153.3
Agriculture	107.0	243.2	136.2
Miscellaneous	14.1	17.0	2.9
Total	3,957.7	6,382.2	2,424.5

Highways, debt, and government absorbed three-quarters of the increased expenditure. Highways received the main benefit of the new expenditure level, accounting for 42% of the increase. Debt was next taking 21%, then government with 11%. The growth of provincial police costs, and of government departments, accounted for the increased expenditure on government. Debt and highways dominated the level of expenditure, and absorbed most of the increases: debt accounted for 32% of the total and highways 30%. Education accounted for 11% as against an average of 18% for all provinces, and welfare for less than 7% against an average of 20% in all provinces. But in New Brunswick new demands were emerging with respect to welfare and education, demands for the establishment of social services on levels comparable to those in other provinces. The Province increased its expenditures

(6) The increased yield of gasoline taxation was partly due to the growth of road traffic, and partly to the increase in tax rate to 5 cents per gallon in 1929.

on public health, and on provincial institutions during this period, but the demand for additional hospital grants, child welfare services, old age pensions, and mothers' allowances was insistent. In 1930 it was decided to institute old age pension payments, but the advent of the depression caused a postponement of payments until 1936. The other welfare services are still on a very modest scale. In education, in 1928 and 1929, the increased expenditures went largely to free school books, but by 1930 this particular expenditure was smaller, and the new education expenses were going also to school grants and teachers' superannuation. Highway expenditures and debt charges, however, so far dominated the expenditure system that concessions to welfare depended almost entirely on the emergence of further revenues.

During the boom, the debt rose by another $15 million. In 1921, 1925 and 1926, the total expenditure (current and capital) had averaged over $5 million but in 1927 it rose to $6.6 million, then to $9.0 million, then to $11.6 million, and in 1930 to $13.9 million, a level not reached again until 1937, when the 1930 peak was exceeded, and the total expenditure reached $17.0 million. The $15 million increase in outstanding debt occurred despite the sale of the Saint John and Quebec Railway to the Canadian National Railways in 1929. The railway was sold for $6 million, of which $2.7 million were paid by the assumption of bonds outstanding. The Province wrote off $2.96 million of the railway investment as a capital loss. The main expenditure contributing to the debt increase was the highway expenditure which approximated $17 million in the boom period, the annual outlay increasing as the boom years advanced, and reaching a peak in 1930 ($6.6 million). In the boom years also, additional investment was made in the power commission, the expenditure beginning to rise in 1930. Even in the boom period, then, the Province was subject to financial pressure in two ways. On the one side, the expenditure needs were

growing; first, through the necessity of maintaining development expenditures and, second, through the new demands for social services that would be comparable in standard to those given by other governments. On the other side, the revenue possibilities were limited, despite the increased Dominion subsidy. Some previous Dominion grants-in-aid (subventions) were tapering off, and the Province's own revenue-raising powers were inherently weak by reason of the lack of diversity in its economy. The need seemed to be to lighten tax burdens, because of the citizens' strong antipathy to direct taxation and because of the apparent lack of an income level among the mass of voters that could provide a taxable surplus. At the same time, the proportion of revenue going to net debt charges (32%) was much higher than in any other province (general average 17%), so that the debt history of the Province was already threatening to dominate the public finance system, and its future direction.

The effect of the depression has been to hasten the forces making for enlargement of the public finance system. It involved a new level of borrowing, mainly for public works, for deficits, for the power commission, and for relief: as a result debt charges rose still higher. At the same time, the costs of welfare in the current expenditures were pushed up: highway maintenance charges have not recovered to their 1930 levels, but in part this was due to the new road programme on capital account. Since 1930, current expenditures have risen by 13% and outstanding debt by 56%. The debt increase may be indicated broadly.

$000

	1930	1931	1932	1933	1934	1935	1936	1937
Current Surplus (+) or Deficit (-)	-79	+13	-189	-785	-361	-432	- 48	+357
Capital Expenditure.	7,492	4,358	1,823	942	1,340	4,031	4,198	9,819
Over-all Deficit	7,571	4,345	2,012	1,727	1,701	4,463	4,246	9,462
Debt Increase	6,446	5,786	1,236	1,815	1,404	4,412	5,625	9,145

The difference between the over-all deficit and the debt growth was due chiefly to changes in advances to utilities, and to instalments received for the sale of the Saint John Railway. The debt growth was attributable, therefore, mainly to the capital works and only about 5% to deficits on ordinary account.[7]

The above table indicates that capital expenditures were contracted greatly in the depression years to 1933, but have since recovered to a new peak. In common with most provinces, New Brunswick felt it necessary to rush for cover in the depression, by cutting expenditures that could be postponed and by raising new revenues.

In 1932 it was decided to attempt to balance the budget, even if that would "impair the efficiency of the services of the province", as the provincial secretary then said. Both ordinary and capital expenditures were curtailed, and taxes were raised in an effort to offset a decline in liquor profits, domain, and licences. The gasoline tax was raised from 5 to 7 cents, and to 8 cents in 1933. Succession duties were raised, and corporation taxes of certain sorts (e.g. banks, insurance) were also added to. The current deficit declined from 1933, and a surplus emerged in 1937. The capital expenditures also expanded greatly from their depression low.

The reduction of capital expenditures from $7.5 million in 1930 to $942,000 in 1933 must have had considerable effect on the economy of New Brunswick. The decline and recovery in capital works occurred as follows:

$000

	1930	1931	1932	1933	1934	1935	1936	1937
Highways	6,593	3,222	1,616	690	1,031	4,732	4,022	9,733
Buildings	598	856	165	143	55	46	67	55
Other Advances etc.	301	280	42	109	254	-747	109	31
Total Capital Account	7,492	4,358	1,823	942	1,340	4,031	4,198	9,819

(7) Between 1930 and 1937, outstanding debt grew by $29.4 million: the current deficits during this period amounted to $1.4 million.

New Brunswick, like other Canadian governments, apparently extends its capital works in the good years. The main highway expenditures of the past three years have been for hard-surfacing. Apart from the above expenditures, advances to the power commission were necessary, these reaching their peak in 1931. In 1932, 1933 and 1934 net losses on exchange involved in all $441,000. From 1931 to date direct relief required financing, with also small amounts for municipal relief up to 1934.

Over the period 1930 to 1937, the government investment in highways was by far the most outstanding capital commitment, the investment increasing by $25 million in these years. The power commission accounted for $3.1 million, and current deficits for $1.4 million. Relief, and investment in buildings, each accounted for $1.4 million, and exchange for $0.5 million. Allowing for the change in surplus account, the write-offs and change in current assets, the outstanding debt rose by $29.4 million. By October 1937, the assets in the provincial balance sheet were as follows:-

		$000
Current Assets		5,321
Utilities		8,154
Public Works		61,796
Relief, (non-self-supporting) loans, etc.		5,159
Capital losses		2,591
Current Deficits		6,940
		89,961
ss Surplus Accounts -		
Sinking fund reserve	7,532	
Capital surplus	354	
Deferred Revenue	112	7,998
Total Outstanding Debt		81,963

In the depression years, the most significant change that has occurred in the revenue system has been the growth of importance of taxation in the yielding of revenues. The changes in gasoline taxes, corporation taxes on banks, insurance and extra-provincial companies, and succession duties have increased their yields beyond the pre-depression levels. Taxes now produce

37% of the revenue as against 25% in 1930, and 22% in 1921. Taxes increased their yield by over $1 million between 1930 and 1937. The other revenues that are now above the 1930 level are licences and subsidies, while liquor profits have failed to recover their previous levels. In the new level of revenue, the outstanding growth has been in gasoline taxes and motor licences, which between them give now 33% of the revenues. The following table shows the main revenue changes in the period 1930-37:

Revenues

	Increase or Decrease 1930-3	Increase 1933-7
	$000	
Subsidy	+ 30.7	+ 269.1
Taxes	+109.0	+1,050.9
Licences	-117.2	+ 130.9
Domain	-322.9	+ 530.2
Liquor	-999.0	+ 559.4

The above table indicates the sensitivity of the liquor and domain revenues in the depression period: the taxes however kept up in this period. In the recovery years (1933-7) all items expanded, the subsidy by reason of the White Commission's recommendations and the tax revenue mainly by reason of the increase in the yield of the gasoline tax, a result of growing use of the highways and an expanding tourist trade. The licence revenues also reflect this change. The public domain reflects the increase in the lumber business in 1936 and 1937., Liquor profits have not recovered to the 1930 levels, despite the fact that 1937 may prove to have been a good "recovery" year. The fact that the recent buoyancy of revenues has been due very largely to new yields from gasoline taxes and automobile licences should indicate that continued expansion of this source of revenue can hardly be expected. In short, the revenue history of the last two years does not

indicate that revenue possibilities have expanded in the province. The revenue basis is still narrow, as it probably must be since the economy is not highly diversified, and since persistent economic difficulty tends to limit the taxable capacity of the people, and to leave few taxable reserves for meeting future needs.

Up to 1936 current expenditures continued to outstrip revenues. Net debt charges continued to dominate the expenditure system, reaching 39% of expenditures by 1937. Other expenditures showed as much growth as the burden of debt and the narrow revenues would permit. Significant was the expansion of welfare expenditures, which formed only 7% of total expenditure in 1930 but rose to 17% by 1937. This growth was due largely to relief expenditures: between 1930 and 1933 welfare services excluding relief fell by $66,000 but then rose again, and the addition of old age pension payments in 1936 raised their total. If relief costs are added to welfare, by 1937 this item had risen to 17% of current expenditures. As a consequence of the increase in debt and welfare, and in keeping with the limited revenues, many other services were contracted. In 1930 highways had accounted for 30% of expenditure, but by 1937 they accounted for only 16%. But since debt, welfare and highways accounted for 72% of the new expenditure level in 1937, it is clear that little increase could be afforded to other services like education, agriculture or domain. There was however a slight increase in domain expenditures. The following table indicates the extent of expenditure changes in the depression and recovery years:

Expenditures

	Increase or Decrease 1930-3	$000	Increase 1933-7
Net debt charges	+ 756.3		+ 16.3
Welfare	+ 409.4		+ 357.3
Education	- 94.6		+ 132.5
Justice	- 154.0		+ 49.2
Legislation	- 32.0		+ 5.4
Government	- 53.6		+ 93.8
Agriculture	- 129.6		+ 104.7
Domain	- 86.8		+ 170.9
Highways	-1,193.8		+ 453.9

Debt and welfare have increased throughout the period. Of those cut in the depression, only education, domain, and government have been restored above their previous levels.

SUMMARY

(1) The New Brunswick economy showed even less resiliency than that of Nova Scotia in the post-war period. The great dependence on forestry and agriculture, neither of which was fitted for any notable expansion, meant that recovery from the 1921 depression was difficult, and in fact in 1928 and 1929, the net production was still near the 1921 level. Thereafter the depression caused contraction. Agriculture tended to decline progressively, and forestry failed to recover to its War levels. The growth of the pulp industry, which was late in the Maritimes, did not provide rural employment opportunities comparable to the lumber industry. The Province has not, as compared with Ontario and Quebec, been getting a high rate of return from its forest resources, and there are indications that conservation and protection costs may be increased in the future.

(2) The debt problem in New Brunswick had been present before the War, and it was attributable largely to the costs of roads and bridges, and to the extension of railway development. The Saint John Railway was sold out to the Canadian National Railways in 1929, and to that extent the burden was lightened. But in the post-war period, the need for highway expenditure, and more recently for the hard-surfacing of highways, and for attention to electric power development, all added to the debt burden. Governments elsewhere, by expenditure on roads, railways, bridges, public works, and by encouragement of agriculture and farm settlement, secured some measure of progressive development, but in New Brunswick the same policy failed to increase income appreciably, and the burden of debt charges has progressively increased, until now the debt charges

account for a very appreciable part of the ordinary expenditures. Next to Saskatchewan, New Brunswick has the heaviest dead-weight debt of all provinces, in relation to revenues. In relation to provincial production, the debt is almost twice as heavy as that for the provinces as a whole.

(3) On education, the Province spends a smaller proportion of its revenues than do others. In 1926, it spent nearly as large a proportion of its revenue as did Nova Scotia, but it has not been able to expand this service, and evidence suggests that any increase in revenue would probably be utilized for the extension of education. Failing further increases in revenue, it may be found necessary to increase this expenditure anyway, as one method of improving the mobility of populations in distressed areas. On public welfare also, the amount spent tends to be a smaller proportion of revenues than in most provinces, and, with the debt burden as heavy as it is, there is a presumption that social services are lagging. The 1936 increase in welfare service was due to the undertaking of the long postponed old age pensions. Rural health services are still lagging, however, and further increases in public health services, as also education, will probably be necessary in the near future.

(4) The revenue system, like that of the other Maritimes, is considerably dependent on the Dominion subsidy. The history of the tax system, also like that of Nova Scotia, has been dominated partly by dislike of direct taxation, and largely by the lack of taxable objects due to economic retardation. New Brunswick, resembling Nova Scotia in not collecting an income tax, fails to impose any general tax on corporate capital, as do Nova Scotia and some other provinces. Accordingly, of the corporation taxes, New Brunswick is greatly dependent on those on insurance and railways. These between them make over 50% of the corporation taxes, the remainder coming from taxes on extra-provincial companies, banks, and telephones. Again New Brunswick, like Nova Scotia, does not

impose succession duties as low in the scale as do the western provinces, but New Brunswick fails to impose the same heavy rates on the high brackets as does Nova Scotia. Accordingly, among the taxes raised, New Brunswick is greatly dependent on the gasoline tax, which forms almost half of the tax revenue. Although the gasoline tax rate is high, the yield is comparatively small, and the same difficulty with respect to yield has been found in the corporation taxes, on which higher rates were imposed in the depression years. Higher licence fees also failed to show any marked buoyancy, except for automobiles. It should be noted also that in 1935 and 1936, the revenues profited from succession duties on two unusually large estates, and that the return from these duties is unlikely to be maintained in the near future. Despite the higher tax rates, the accident of high succession duty yield in 1936, and the advanced stage of economic recovery in 1937, the revenues just covered expenditures in 1937, and some expenditures had not regained their former level. So far, economic conditions permitting an enlargement of certain expenditures have not emerged, the technical position of the budget has not improved, and the debt growth has tended to be persistent.

(5) The long run financial position in New Brunswick is unlikely to be easy, partly because, as in Nova Scotia, there is little likelihood of there being any marked "frontier" expansion, and partly because the economy is even more narrowly circumscribed than that of Nova Scotia. The existent burden of debt, due only in small part to the recent depression and bound up more with the long-term fundamental needs of the province, is already onerous, and its existence may limit the Province's ability to encourage more intensive development of existent resources. Ordinary expenditures on education, welfare, and public works may also require to be increased for social, as well as developmental, reasons.

The Financial Position of Quebec

Certain geographical, historical, and institutional features of the Province of Quebec have proved significant in the course of the provincial finances.

The geographical factor of most significance is the St. Lawrence river. As a trade route between the Great Lakes and the Atlantic, the main stream determined the entrepot position of Montreal, and even in the pre-Confederation period lines of development tended to converge there. After Confederation, the provincial government encouraged railway building in the settled regions of the Province, while Dominion expenditures on railways, canals, and harbours in later periods further strengthened Montreal's position. The river, by providing trade routes, was important in determining the original areas of settlement, of agriculture, and of forest exploitation, while its tributaries, especially in the later period of hydro-electric energy,[1] have helped to bring about a fairly large range and volume of manufacturing in this region. Easy transport facilities and cheap motive power have combined with satisfactory labour conditions, and the stimulus of tariff policy, to increase the volume of manufactures. While the main stream of the St. Lawrence river provided sites for the commercial and manufacturing activities of the Province, its tributaries provided the means of exploiting and exporting the Province's natural resources - forests, pulp, power and agriculture. And the Gulf gave rise to the Gaspe fisheries.

As Winnipeg became the entrepot of the prairies, Montreal tended to become the entrepot of the whole Canadian economy. Its prosperity depended on the home and foreign trade of Canada as a whole, a condition that sometimes added greatly

(1) Quebec now leads all provinces in potential and developed water-power, having 39% of Canada's potential horse-power, and 49% of the existent Dominion turbine installation.

to the revenues of the Province. In periods of economic dislocation, however, the responsibility for the maintenance of this commercial and manufacturing "overhead" of the whole economy would tend to fall on the provincial institutions, (provincial and municipal governments, charitable institutions, etc.), a cost that became increasingly onerous as the entrepot characteristic developed, and as social philosophy began to dictate new ranges of governmental expenditures in depression periods. The ability of provincial institutions to meet these costs depended on their inherent resources (in funds, revenue possibilities, credit, etc.), and on the frequency of serious dislocations involving them in new debt.

The commercial and manufacturing activity of Quebec increased rapidly in the 20th Century, and has been accompanied by a large transference of people from the country to the town. Growth of the pulp and paper industry and intensive utilization of the Province's waterpowers drew workers to certain rural areas, and both government and church have always been concerned with colonization and rural development. Nevertheless, in the last forty years, there has been on balance a marked transference of population from rural to urban areas, and a growing concentration in the Montreal region. In 1891 urban areas accounted for only 33% of the total population, but by 1931 they held 63%. This migration affected both rural and urban organizations, institutions and services(education costs, charity, church, as well as housing, road programmes, etc.). Even more significant than the population shift itself was its centralizing character. Over 40% of the people of the Province are now found in the two cities of Montreal and Quebec. In relation to the size of the settled part of provincial territory, this urban centralization, and its economic dependence on the total Canadian income, creates a population structure that has no counterpart elsewhere in Canadian provinces.

The second determinant of the region's economic expansion was the distinct racial and religious character of the majority in the Province. This determined the nature of the institutional structure, and the place of the government in economic development. In both these respects Quebec has been unique among the provinces. Since these characteristics of race and religion were regarded as fundamental in themselves, it was to be expected that the provincial government of Quebec would be less concerned than most provinces with matters of economic change, taxes, and finance.

And broadly the financial history of the Province bears out this expectation. From the distribution of provincial government expenditure at the outbreak of the War it is evident that the Province was concerned primarily with the functions considered "necessary" by John Stuart Mill. Quebec spent more of her revenue on justice, legislation and general government than did the other provinces. At that time also Quebec tended to spend more on debt, being concerned with the reduction of the debt that had been incurred for railway-building in the last quarter of the 19th Century. Quebec was not, at this time, (1913) embarking on new undertakings, supplying utilities or loans, as were the other provinces. In 1913 Quebec spent less than other provinces on welfare and on education, but this was due, in large part, to the fact that these services were also provided by the Church in Quebec. At this time also, Quebec's expenditures on highways were small but the inauguration of the good roads policy in 1912 indicated that Quebec's highway expenditures were likely to expand. Nevertheless, through the late 19th Century, and up to the War, when other provinces were undertaking new enterprises of various sorts, Quebec confined itself primarily to the traditional necessities of government, and did this in a conservative way. Economic development was left to private enterprise, and welfare and education largely to non-government

institutions.

The financial history from the late 19th Century onwards may be contrasted with that of the '70's and '80's. In that earlier period, Quebec gave much attention to the works that seemed necessary for developing the territory adjacent to the St.Lawrence river, and a very positive policy of railway encouragement was followed. That policy was in contrast to that of Ontario at that time. Unlike Ontario, Quebec did not lie directly between the seaboard and the western states (both U.S. and Canadian), and the privately provided railway mileage in Quebec tended to be small. Quebec therefore, aided private construction by subsidies, and when the railway being built through Quebec, Montreal and Ottawa encountered financial difficulties, the Quebec government took over construction of the line (1875). It was completed by 1879, and the government operated the railway until 1882 when it was sold in part to the Canadian Pacific, and in part to the North Shore, Railway Companies.

The following indicates the extent of the railway encouragement by the government in the decade following 1875.

	Subsidies to various railways	Subsidies and costs of construction of Quebec, Montreal and Ottawa Railway.	Total for Year
		$000	
1875	359	651	1,010
1876	196	1,322	1,518
1877	279	3,203	3,482
1878	464	2,146	2,610
1879	403	1,901	2,304
1880	233	268	501
1881	216	2,206	2,422
1882	74	837	911
1883	99	583	682
1884	137	438	575
Total 1875-1884	2,460	13,555	16,015
Total 1874-1900	12,221	13,956	26,177

Of the $14 million spent on the Quebec, Montreal and Ottawa Railway, the Province recovered $10.4 million, consisting of $7.6 million from the sale, $2.4 million from the Dominion government as a grant for the construction, and $0.4 million from construction refunds. These proceeds were subsequently applied to the redemption of provincial debt.

As a result of this policy of railway encouragement,(2) Quebec had to resort to borrowing from 1874 onwards, and debt charges rose, accounting for over 50% of the increase in current expenditures between 1869 and 1900. By 1900 most of the then outstanding $35 million of Direct Funded Debt had been incurred for railway purposes, although few other expenditures - such as public buildings, bridges, etc., which grew with the 40% expansion of population between Confederation and 1900 - were also financed by loans. Deficits that arose from the failure of revenues to keep pace with the new expenditures also required financing by loans.

In 1873 Quebec had no debt commitments; by 1880 debt charges accounted for 23% of her total expenditures: by 1900 the figure had risen to 33%. This growing burden was heavy in this last quarter of the century, especially when revenues did not seem buoyant. Accordingly, only necessary capital works (public buildings, bridges, and colonization roads) were permitted, and the revenue basis was widened by the adoption of corporation taxes in 1882,(3) which began to produce revenue in 1888 after their constitutionality had been upheld by the Privy Council. But debt charges and economic depression continued to produce deficits even after Quebec followed Ontario in the adoption of succession duties in 1892. A new revenue basis, however, was present, and was able to yield buoyant returns in the boom that began after 1896. Until then, receipts from the public domain and the federal

(2) Quebec's railway mileage rose from 575 in 1867, to 3,400 in 1900.

(3) Quebec was the first province to resort to direct taxation in this form.

subsidy had constituted the main part of the revenue system although their importance was declining. Together they formed 84% of the total revenue in 1869, but by 1900 only 55%.

Quebec Revenues 1869 and 1900

	$000 1869	1900
Public Domain	391	1,311
Federal subsidy	980	1,087
Liquor control	70	537
Interest, etc.	12	514
Licences, fees, etc.	156	384
Miscellaneous	14	44
Direct taxation	-	459
Total	1,623	4,336

After the adoption of the policy of railway encouragement, Quebec, like the Dominion and some other governments, altered its expenditure policy. No new commitments that would lead to new debts were undertaken, and the revenue basis was widened to try to curtail the deficits that had become too frequent, according to the opinion of the time, and had tended to be large from 1877 to the end of the century. Unlike other Canadian governments, however, Quebec persisted in this policy even in the peak years of the boom before the War and even in the post-war booms. The result was, as Quebec industry developed in this period and revenues were buoyant that after the turn of the century and during the boom Quebec enjoyed a long series of surpluses unique in Canadian public finance. The other side of this policy - the avoidance of important debt growth - was also unique, so that Quebec, which had been heavily burdened with debt after her railway policy in the last quarter of the 19th Century, had by 1930 a debt charge that was insignificant as compared with the other Canadian governments.(4) This transition

(4) In June 1937, Quebec's outstanding debt reached $236 million, but almost 60% of that was added after 1930.

in Quebec's fiscal policy (and financial position) after the "railway period" is explainable largely by the government's unwillingness to embark again on enterprises that would create debt. This unwillingness was partly due to Quebec's particular interpretation of the place of the state in the life of the community, and partly to favourable circumstances that produced economic expansion by private enterprise and so gave rise to no demand for an active government policy. In the era of expansion the Dominion government was attending to the provision of equipment (National Transcontinental Railway, Harbours, etc.) and private enterprise was developing the manufacturing and commercial activities of the Montreal district. Private capital and enterprise supported also the development of the forest industries, and the concomitant pulp and power industries, the state concerning itself only with regulation (e.g. in 1910 the imposition of restrictions on the export of unmanufactured pulpwood cut on Crown lands). In these conditions, Quebec's financial position was unique at the beginning of the War, with its tendency to falling debt, its conservative method of finance, its connections with the Church for education and welfare services, and its unwillingness to reduce direct or other taxation in the expansion, preferring to apply excess revenues to necessary capital works and so to reduce the volume of loan operations.

In the pre-war boom therefore, economic conditions rendered more easy the government's adherence to its Gladstonian financial policy. Between 1900 and 1914 capital invested in Quebec's manufactures trebled, field crops doubled in value and there was a rapid growth of trade through Montreal. Of outstanding importance was the expansion of hydro-electric undertakings,(5) and the new importance of the pulp and paper industry with the growth of American demand. This new industry received an extra

(5) From 83,000 h.p. in 1900 to 664,000 h.p. in 1914.

stimulus through the removal in 1913 of the United States tariff on newsprint. As a result of economic development, revenues became more buoyant, particularly the new direct taxes on corporations and on inheritance, as the following table shows:

	Year ended June 30 1900	Year ended June 30 1914
	$000	
Direct Taxes:		
Corporations	187	943
Succession Duties	271	1,605
Other	1	54
Total Direct Taxes	459	2,602
Federal Subsidy	1,087	1,969
Public Domain	1,311	1,866
Licences, etc.	384	1,114
Liquor Control	537	794
Interest	514	145(6)
Miscellaneous	44	274
TOTAL REVENUE	4,336	8,764(6)

Revenues doubled in the boom period, but the main growth was in the yield of the direct taxes. These had increased almost six-fold, and ascended to first place in the revenue picture. The other large increase came from licences, fees, and fines. Federal subsidies had been increased as a result of the 1907 and 1911 revisions and public domain had yielded more as a result of the new exploitation of forests. Nevertheless these two items, which had yielded 84% of the total revenue after Confederation, by 1914 yielded only 44%.

The expenditure position at the outbreak of War also indicated changes due to economic development, and the Gladstonian policy of the Quebec government. The following table indicates the expenditure position:

(6) Includes interest receipts of $87,000 which were deducted from Debt Charges in the statistics prepared by the Director of the Public Accounts Inquiry.

	Year ended June 30 1900	1914
	$000	
Justice	682	1,257
Government	492	1,029
Legislation	200	424
Domain	339	738
Education	471	1,488
Welfare	343	515
Debt	1,538	1,053(7)
Highways	5	893
Agriculture	174	421
Miscellaneous	73	413
TOTAL	4,317	8,231(7)

The greatest percentage increase in expenditure had been in highways, as a result of the new road programme of 1912, although the amount spent on this item was not yet important. Before 1912, the provincial government's interest in highways had been confined mainly to colonization work. In 1914, education was the largest single item, and its increase was due partly to the increase in school population, and partly to the improvement of educational standards. Justice, government and legislation absorbed 33% of total expenditures.

But Quebec's ability to maintain its budgetary policy was threatened in several ways. Continuance of economic expansion at a high rate was unlikely: even more important, the nature of 20th Century expansion was creating its own problem of rural-urban transference of population. These conditions alone were likely to create new expenditure needs in the Province. Furthermore, changes in techniques (e.g. road transport) and the stimulus given to these changes by road programmes in other provinces were likely to induce similar works in Quebec. Lastly, the changes in social philosophy which were common to all countries, and which would be hastened by any change in the rate of economic progress,

(7) In the statistics prepared by the Director of the Public Accounts Inquiry interest receipts amounting to $87,000 were deducted from Debt Charges in this year.

were not likely to leave Quebec unaffected. Some of these factors began to affect the budgetary position at the outbreak of War, others more noticeably in the dislocations that followed the War, while all gained in importance in the depression after 1929. It is after 1929 that the budgetary position shows most clearly a tendency to move in the same direction as those of other provinces, the signal changes in the Quebec position being the growth of debt and the provision of new or enlarged services. But it is important to recognize that the factors making for change have been operative since the War at least.

Up to the War, the expenditures had followed well-defined trends, in keeping with the government policy. The costs of governing (justice, government and legislation), which have always been relatively high in Quebec, responded to the growth of population and economic expansion, the rate of increase becoming greater after the pre-war boom gained impetus (i.e. after 1905), and maintaining itself into the recent depression (1933).

Debt charges, as already indicated, rose rapidly to 1900, but government aversion to borrowing had made them a relatively small item by 1930. Provincial expenditures on education rose at about the same rate as the costs of general government, legislation and administration of justice. Public domain expenditures also rose at the same rate until after the War when they grew more rapidly as a result of new expenses incurred in handling the natural resources. Public works and welfare expenditures both grew more rapidly than other services, particularly after 1914, and deserve somewhat more detailed mention.

The enlargement of the scope of provincial government activities may be timed from the emergence of the good roads programme in 1912. Up until then, especially after 1905, the various services - government, education, domain and welfare - had all moved together roughly in response to the general economic

expansion and the growth of population. It was public works expenditures, however, that indicated the new line of expenditure growth. The capital expenditures on public works rose from about $200,000 in 1910 to over $7 million by 1930. Before 1912 the Province had done little more than attend to colonization roads, most of the road work being done by the municipalities, and in June, 1914, only $3.3 million of the total public works assets of $14.3 million had been invested in highways.(8) It was not until the Good Roads Act of 1912 that the provincial government admitted the necessity of aggressive development and co-ordination of the highway system. This Act allowed the Province to construct new roads, and to make grants to municipalities to induce them to improve local highways. The municipalities were to pay 2% per annum to the Province on the amount of the grants. (This charge was raised to 3% in 1916, reduced to 2% in 1928, then to 1% in 1931, and then abolished.) The government was originally authorized to borrow $10 million for the purpose of this Act, an amount subsequently increased. As traffic increased, and road mileage expanded, the poor standard of municipal road maintenance became an important issue. The Province in 1916, by another Act, gave subsidies to municipalities for maintenance and authorized the provincial department to maintain improved roads at the cost of the municipalities should they neglect to do so. In 1917 there were 2,000 miles of improved roads in Quebec. While the department made every effort to get municipalities to maintain their improved roads, it is estimated that not more than half of them performed the standard maintenance work. In 1921, the legislature tried further to improve the system by creating regional highways at the joint expense of Province and

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(8) e.g., in the Act of 1907 which permitted grants to municipalities of yearly subsidies équal to one-half the expenses incurred on roads made and improved.

municipalities. In 1922, the entire cost of these regional roads was taken over by the Province, and this went far to solve the question of road maintenance. By June 1922, the provincial investment in roads reached $31 million (as against $3.3 million in 1914), and roads had become the outstanding government investment. The final solution to the road maintenance question was reached in 1927, when the Province took over the maintenance of all roads. By then the improved mileage was approximately 8,000 and the provincial investment reached $49 million. The next step in the provincial highways policy was towards the modernization of roads, begun in 1929 and involving heavy capital expenditures for widening and paving. Annual government investment in highways has been particularly high since June 1929. About $50 million, or about one-third of the total new debt accumulated in 1928-36 was spent on highways. Part of the expenditures on relief works, toll bridges and colonization undertaken in this period also improved the highway system. By 1937, there were over 17,000 miles of improved roadway in the Province, 97% of which were maintained by the provincial government. The following table indicates the annual government investment in roads from 1929, with the current expenditures, and current revenues from licences and gasoline.

HIGHWAYS

Year ending June 30	Capital Expenditure	Current Expenditure	Revenue from Gasoline Tax and Motor Licences
	$000,000		
1930	6.0	8.2	9.2
1931	5.2	9.5	9.8
1932	9.7	6.6	10.4
1933	5.7	5.0	9.9
1934	3.6	5.4	10.0
1935	2.9	5.4	10.6
1936	7.2	7.1	11.7
1937	5.8	6.0	13.0

Total Provincial Highway Asset 1937: $100.5 million.

From the above table it is clear that the expenditures (capital and current) reached their peak in the year ending June 30, 1932, declined in the depression, but have recovered in 1936 and 1937. The policy of modernization has been resumed, the latest appropriation for a special roads programme being passed by the legislature in 1938. This appropriation, supplementary to normal expenditures, amounts to $50 million, and is to be spent over a four-year period. In 1912, when the Province was faced with the choice between possible economic retardation through inadequate roads, or possible economic advancement through a vigorous highway programme, the latter line of action was taken. But the same question faced the Province again on the eve of the present depression, when road modernization seemed necessary for economic advancement. A still more vigorous policy was then adopted, only to be relaxed in the depression. Now it is apparently being pushed to its logical conclusion.

As a result, highway expenditures after 1912 tended to take a larger proportion of current revenues. In 1913 they absorbed less than 11% of the current expenditure, by 1925 they took 15%, by 1929 24%, and by 1930 24%.

Quebec is breaking with tradition in a second policy designed to promote technical progress. Previously the Quebec government concerned itself in rural development, and in utilization of mineral and forest resources, only so far as to provide facilities for private enterprise. At present the government is taking a more positive line. It has acted vigorously to assist mining and colonization, appointed a provincial electricity board and expanded the public works programme. These policies, as well as the highway programme indicate how the depression has changed the place of the government in the Quebec economy.

While some of these government activities are of recent innovation, some had their roots in events that occurred

before the depression. The peculiar features of the Quebec economy had been emphasized by the developments of the War and post-war periods. The War promoted unusual activity in certain industries, stimulating the production of articles previously imported, creating a financial as well as a commercial centre in Montreal, and providing considerable impetus to the rural industries of the Province. Agriculture was expanded[9] to meet War demands, and post-war readjustment to more normal requirements created considerable economic distress in rural areas. At the same time certain other industries, especially the pulp and paper industry, expanded rapidly, even after the War. By 1926, the pulp and paper industry was the largest industry in Quebec.[10] Hydro-electric development roughly paralleled the pulp and paper industry, and by 1926 the turbine capacity had reached 1.9 million horse power, about three times the pre-war capacity. In sharp contrast to Ontario, the Quebec government at this time made no attempt to enter the power industry.

The net result of the economic development in the War and post-war periods in Quebec was to enlarge certain industries greatly. Quebec's outstanding industrial characteristic is not, however, diversification but rather dependence on a few important manufactures, such as pulp and paper, cotton and cloth, cigars and cigarettes, boots and shoes, and railway rolling stock. Industrial growth thus meant great concentration in certain localities, while new centres grew near power developments. One-industry towns appeared and urban population began to outnumber rural. These characteristics of the economy did not appear as disadvantages in prosperous times, but in depression they created difficulties. Serious problems of relief and maintenance arose not only in the one-industry towns, always liable to dislocations, but in the large manufacturing centres as well.

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(9) Areas seeded to field crops had been less than 5 million acres before the War but reached 8 million by 1921.
(10) Its gross value of production had increased from $45 million in 1917 to $107 million by 1926, and its investment and its production of paper had increased by 200% in the same period.

Thus the depression revealed the effects of migration from the country to towns, and the apparent need to encourage rural development as an offset to urbanization. In these conditions, the emergence of a more positive policy of rural development, extensive colonization, highway work, and mineral development in the north-west, were to be expected.

The government and the Church have always been concerned in colonization, but the government tended to concentrate its efforts on colonization roads in the pre-war period.(11) After 1914, however, the Province undertook to encourage rural settlement by publicity, sale of lots at low prices, distribution of seeds, and grants for roads and school chapels. The extent to which this policy was successful was hidden by the events of the War, which not only stimulated industry but induced a great extension of agricultural acreage. High agricultural prices that ruled until 1920 encouraged rural life, but the subsequent collapse of prices, the agricultural depression and the revolution in farm methods that took place in the specialized agricultural provinces, all intensified agricultural difficulties in Quebec, except for those communities that found markets in the growing cities of the Province. In the post-war period, the ordinary expenditures on colonization were supplemented by expenditures of $7 million on capital account. These funds were used for colonization roads, and for aids to schools in such areas.(12) In addition to these grants, the government encouraged colonization after 1923 by premiums for clearing the land and for its first ploughing. By 1931, however, it was obvious that the previous boom had intensified the transference from rural to urban areas, and when the boom broke, the need for redressing

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(11) From Confederation to 1914, the provincial government colonization grants amounted to $5.5 million, and were charged mainly to current expenditures.

(12) The areas of new settlement in the 20th Century were mainly in the north-west of Abitibi and Temiscamingue, the Saguenay regions of Lake St. John and Chicoutimi.

the population balance was more evident than ever. It was necessary to relieve both rural and urban unemployment, and in any case rural development appeared a desirable end in itself. From 1925 to 1930 no colonization work was financed by loans, although ordinary expenditures on colonization rose by 78%. The events of the depression, induced some changes in provincial colonization policy. "We have set out on new trails" according to the report of the Minister of Colonization in 1936. A series of Acts mark the new direction. In 1932 the Minister of Colonization was authorized to purchase municipal property at tax sales, if the property could be used for colonization. It was in 1935, however, that the major steps were taken,and colonization came to be regarded as a partial solution to the permanent problems arising from lack of balance in the rural-urban distribution of population. Expenditures on colonization of over $5 million capitalized by the Province, were made in year ending June 1936, and almost $6 million in year ending June 1937.

Coupled with the colonization work at present is new expenditure to assist agriculture (e.g. distribution of seed grain) in the ordinary account. More significant was the innovation in 1936 of the Quebec Farm Credit Bureau. The Bureau was authorized to borrow up to $10 million to finance loans to farmers and if necessary purchase property. Loans are secured by a first mortgage on farms, are limited to $6,000, bear interest at 2½% per annum, and are repayable either over 30 years, or over 39½ years. The Bureau may advance funds also on security of second mortgage. The Quebec Farm Credit Bureau's borrowing authority was raised to $15 million in 1937, and to $25 million in 1938. In March 1938, the Provincial Treasurer announced that 26,000 applications for farm loans had been received, that $9 million had been lent, and $6 million more of applications accepted.

Development of other natural resources, particularly hydro-electric power, has hitherto been almost entirely in the hands of private enterprise. But there is evidence that the government has recently given its natural resources attention beyond conservation, and that development of resources is beginning to receive new emphasis. The legislature has passed Acts that would permit public authorities to embark on the operation of hydro-electric undertakings. The establishment of the Provincial Electricity Board, with full authority to regulate all phases of that industry, is probably significant. The recent announcement that the government intended to promote the Noranda power development is further evidence of the emergence of a more positive government policy towards hydro.

With respect to mineral development, which has been perhaps the most significant of the recent economic changes,(13) the provincial government's policy has been confined mainly to colonization work, and assistance towards communications. The colonization work in the Abitibi-Temiscamingue area was originally for agricultural purposes, but since 1926 this area has become one of Canada's new frontiers. The Province contributed to colonization projects and road building in the Noranda region. These mining developments are reflected already in the provincial revenues, by rising yields from the levy on mining profits. From $90,000 in 1925, this levy reached $1 million in 1936, so that the present and future development of this frontier is important not only for economic progress in general but directly for provincial revenues. The need of the mining and metallurgical industry for motive power and roads may therefore be connected with the crystallization of government policy towards roads, power, and rural development.

(13) Quebec Mineral Production

$000

Year	Gold	Asbestos	Copper	Silver	All Minerals
1926	76	10,095	369	233	25,740
1929	1,877	13,172	10,020	431	46,455
1933	10,950	5,211	5,214	178	28,164
1937	24,913	14,505	12,379	408	65,044

The change in Quebec developmental policies in recent years has been accompanied by a change in policy with respect to public welfare. Before 1921 the Province made annual grants to mental institutions, and to certain health and charitable purposes, but the main stream of provision for indigents was directed by the religious communities. The enlarged scale of expenditures on welfare in all Canadian communities during and after the War, and the economic dislocation subsequent to the War, so far strained the operation of the Quebec welfare structure that the Province in 1921 had to give special attention to the question. The Bureau of Public Charities was created to assist the indigent sick kept in public charitable institutions. The government was to pay one-third of the patient's costs, and the remainder was to be left to the municipality and the institution concerned. No allowance was made for the capital requirements of such institutions, but this defect was remedied in 1924. The fund was originally derived from the amusement taxes. In 1927 an additional tax on meals in hotels, etc. was added to supplement the fund. Up to 1929, the fund accumulated an operating surplus, but it was then apparent that when all subsidized bond issues became outstanding the fund would require additional resources. The government then enacted legislation making an annual grant to the fund of $1 million from the Liquor Commission. This has been granted in each year since 1929, with the exception of 1932 when $300,000 was given. In the depression, however, when the fund encountered financial difficulty, the amusement and meal taxes had to be raised, and assistance had also to be given from the consolidated revenue fund of the government. In 1935, the consolidated revenue of the Province became liable for capital grants chargeable against the fund. By June 1937, the accumulated deficit of the fund amounted to $7.8 million, and advances from the consolidated revenues totalled $9 million. In June 1937 the Province's indirect liability to

pay interest and provide sinking funds on the bond issues of hospitals and charitable institutions was $15.6 million. The rate of interest on these was probably at least 1% above that payable on the Province's own bonds. As 1935 legislation made the government responsible for the fund's commitments, the segregation of the operations of the fund from the other financial activities of the government may be only temporary until the full transition is completed.

Other welfare services - public health, labour department, and mental institutions - have expanded and in 1936 the old age pensions were added, Quebec being the last province to undertake this service. Although the character of the religious institutions in Quebec had always modified the need for state welfare service, the change in social philosophy in the War period, the extensive centralization of urban populations, and the tendency in depression for the real costs of the urban structure to become money costs for relief have made the welfare question so important as to call for provincial government action. Welfare costs other than relief have risen fairly rapidly in Quebec so that the proportion of its net revenues that the government spends on welfare is becoming more closely comparable with that of other provinces. If relief costs are added to welfare, Quebec at present tends to spend relatively more on this item than do the provinces as a whole. Neglecting relief costs, however, the welfare expenditures have grown as follows:

Welfare
$000

	1921	1929	1933	1936
Health	197	521	695	727
Mental Institutions	341	979	937	1,311
Charity	387	1,529	4,102	4,402
Old Age Pensions	-	-	-	1,828
Labour	80	379	479	694
Other	52	161	291	387
Total	1,057	3,569	6,504	9,349

Between 1921 and 1929 welfare expenditures grew only slightly more quickly than total current expenditures: in 1929 they formed 10% of the total current expenditure, but by 1936 (excluding relief) they had risen to 16%. The main items contributing to the growth were the expenses on charities, and the innovation of old age pensions in 1936. The other items, health, labour and institutions, all reveal an upward tendency.

Despite the changes that the War and the post-war period had involved for Quebec in the extension of developmental and welfare policies, it is still accurate to say that, at the advent of the depression after 1929, Quebec's financial position was particularly strong. The outstanding debt of $96.9 million (June 1930) had not increased in the boom period, as had the debt of all other provinces; - in fact, it had declined a little. The debt charges (less interest received) were only 6% of the expenditures, a percentage much below that in any other province, and only one-third the percentage for all provinces. The government had undertaken only what seemed absolutely necessary investments, and most of the debt represented public works, with small amounts for the charities fund and colonization, and the university grants. The Province had enjoyed a long and, for Canada, a unique series of budgetary surpluses.

The depression after 1929 imposed a double set of disturbances on the economy of Quebec. On the one hand, the exports of the Province suffered - forestry, paper, and power, in particular, and on the other, the commercial and manufacturing activities of the urban population were restricted. For Quebec, therefore, the relief question was a question of supporting rural as well as urban unemployed. From 1930 onwards, over $60 million have been spent on relief, two-thirds of this being for direct relief and the remainder for relief works and grants to municipalities. The annual expenditures were as

follows:[14]

Relief

$000,000

Year ending June	1931	1932	1933	1934	1935	1936	1937
Direct Relief and Municipal Works	.3	4.0	4.7	7.2	10.0	9.2	10.3
Provincial Relief Works	.7	5.0	2.2	1.3	1.2	1.3	4.2
Total	1.0	9.0	6.9	8.5	11.2	10.5	14.5

Between 1930 and 1936 the relief expenditures amounted to $61.6 million, all of which was capitalized. Relief, therefore, accounted for 47% of the debt increase between 1930 and 1936, the increase having been approximately $131 million. Highways accounted for another 27% of the debt increase, and the remaining 26% went to colonization, grants to charities, the Farm Credit Bureau, building, etc. As a result of the very rapid debt growth since 1930, net debt charges (excluding sinking fund requirements), which had formed only about 6% of total expenditure in 1930, had by 1937 (June) increased to about 9%, despite a considerable reduction in interest rates. This proportion is still small compared with most provinces, but nevertheless it has grown fairly rapidly, and seems likely to continue growing for some time, as a result of the more vigorous policies now being pursued by the government.

In the depression years, revenues fell from their 1929 peak to a low in 1933, and last year had not recovered to their 1929 level. Expenditures on the other hand rose comparatively steadily, resulting in a series of deficits on ordinary account that reached $15.6 million in 1937 (June). Expenditures on capital account were reduced to low levels in 1933 and 1934, but have again risen so that the over-all deficit has increased in the last two years.

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(14) This table omits agricultural relief in the form of distribution of seed grain.

Over-all Deficit
$000,000

Year ending June	1931	1932	1933	1934	1935	1936	1937
Current Deficit x	3.0(s)	5.2	12.2	15.3	13.9	15.3	15.6
Capital Expenditure	12.7	16.2	8.7	5.7	3.8	8.5	10.3
Over-all Deficit	9.7	21.4	20.9	21.0	17.7	23.8	25.9

(s) Surplus
x Includes colonization expenditures capitalized.

The steep rise in capital expenditures in the last two years was due, mainly, to an expansion of public works, especially on highways. Highway expenditures had been $9.7 million in 1931, had fallen to $2.9 million by 1934, but by 1936 were up to $5.8 million. Relief works showed the same characteristic, falling from $5.0 million in 1931, to $1.2 million in 1934, and rising again to $4.2 million in 1936. The expenditure on public buildings is still far below the pre-depression level.

In the ordinary expenditures the significant recent changes have been in welfare (including direct relief) and in debt charges. The following table indicates the extent of the change:

Ordinary Expenditures
$000

	Year ending June 30 1931	1937	Percentage Increase
Public Welfare	5,511	19,627	256
Net Debt Charges - Interest	2,087	5,577	167
Highways	9,537	6,022	37 (d)
General Government	3,902	4,734	21
Education	4,965	4,602	7 (d)
Public Domain	6,126	9,834 (a)	61
Justice	3,737	3,399	9 (d)
Agriculture	2,616	3,103	19
Legislation	869	1,191	37
Miscellaneous	743	976	31
Total	40,093	59,065	47

(d) Decrease
(a) Includes capitalized expenditures on colonization.

The outstanding increases were in welfare and debt charges, but a significant decrease occurred in highways. The highway expenditures in the pre-depression period were met largely from current account, but by 1937 the capital expenditures on highways, including the relief works, meant that the government was spending considerable sums on this item, although the current highway expenditures were below the 1931 peak.(15) The decrease in public domain was due largely to a reduction in fire-ranging expenditures: the current expenditures on colonization had also contracted, but as in the case of highways, this was counterbalanced by increased capital expenditures.

In response to the changes in policy that began during the War and have been significantly advanced during the recent depression, the public finance system of Quebec is in a period of transition, although its previous characteristics are still clearly discernible. The percentage of net revenue spent on government as a whole is still considerably higher than in other provinces. The percentage of net revenue spent on domain and agriculture still tends to be higher than in other provinces, as does also the public works current expenditures. At the other extreme, the cost of debt is still a lower percentage of net revenue than elsewhere, as is also the cost of education. Public welfare apart from relief costs still tends to be below the general average, although it is rising. But if the more positive policies of capital works and development of natural resources continue to be pushed as they have been recently, the growth of debt charges alone will probably necessitate some readjustment of the expenditure items in the budget, and even perhaps of the tax system. Even given full economic recovery to levels comparable to those of 1928-29, many of the recently

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(15) A noteworthy aspect of the decline in highways current expenditure was the discontinuance of highway grants to municipalities from 1932 to 1936. In the year ended June 30, 1931 these had amounted to $1.3 million. In 1937 they were resumed on a limited basis.

instituted governmental services (including the servicing of larger debts), will remain to create an ordinary expenditure level considerably above that of the pre-depression years. The full extent of the expenditure changes, and the future level of expenditures, depends on the direction taken in this rapid transition period in Quebec's developmental policies.

On the revenue side, there was a steady increase in the boom period after 1925. In 1930 ordinary revenue was 61% above the 1925 level. In the depression, however, revenues fell by 29% between 1930 and 1933, although the 1933 level was still 15% above that of 1925. In the recovery period after 1933, the upward trend was resumed, and in 1936 revenues were 42% above the depression low of 1933. In 1936 they were 62% above the 1925 level.(16)

In the 20th Century, Quebec's revenue system reflected the growth of manufacturing activities in the Province, direct taxes becoming an increasingly important contributor to total revenues. While some part of the increased return from corporation taxes and succession duties was attributable to changes in rates, especially during the War, the main factor contributing to the rise of these taxes, up to the depression, was the expansion of business and corporate enterprise. In 1900, direct taxes formed only 10% of total revenues, but by June 1937 they yielded about 43% of the new levels of revenue, the dominant yield coming from the corporation taxes. The tax on the capital stock of companies formed the largest part, although since the profits tax was imposed in the depression, it has become an important contributor to corporation taxes. No striking changes were made in the corporation taxes in the boom years after 1925. These, like the succession duties, expanded their yield chiefly in response to the growing concentration of corporate enterprises in the Ontario and Quebec regions. The growth of Canadian manufactures, and of financial and commercial institutions,

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(16) In Ontario the increase in the same period was 152%.

combined with their tendency to become centralized in these provinces in corporate or trustified forms, yielded a persistent increase in corporate capital, and in income liable to inheritance duties. In the post-war period and particularly in the years from 1924 to 1928, the percentage annual increase in Quebec manufactures was paralleled by an almost equal percentage annual increase in the yield of corporation taxes. However, in the post-war period, the most significant change in the revenue system in Quebec was in the Liquor Control profits. The government monopoly of retail liquor sales, initiated in 1921, and the imposition of a 5% tax on purchases of beer from brewers, gave new importance to liquor revenues. In 1913 they yielded only 9% of the total revenue, but by 1925 the proportion had risen to 22%, the percentage rise in liquor "profits" being steady and high until 1929. Again the introduction of the gasoline tax (2 cents per gallon) in 1924, along with the imposition of special taxes for the public charities fund, all added to the revenue growth.

In this period, the tax history of the Province of Quebec was probably unique in Canada. The rise in revenues was faster than in other provinces, due partly to the rise in provincial income which reflected itself in increased corporate investment and therefore larger corporation taxes, partly to the increased utilization of resources and therefore larger revenues from Crown lands, licences, fees, etc., partly to the increased motor traffic and therefore larger returns from motor licences and gasoline taxes, and partly to the increased general spending and therefore larger revenues from liquor sales and amusement taxes. But while the growth of income was rapid, the noteworthy feature was the maintenance of tax rates in face of the buoyancy of revenues. In similar conditions most Canadian governments, including the Dominion, tended to lower tax rates. In contrast Quebec, in which provincial taxes per head were very

low, tended to maintain tax rates, and to continue obtaining annual current surpluses as had been the practice from 1899. Thus, although the expenditures were rising, (by 82% between 1925 and 1930), the Province was able to keep her small debt stationary, and to strengthen the already comparatively strong sinking fund provisions. Gasoline taxes were raised by 66-2/3% in 1928, the security transfer tax raised, and a tax imposed on restaurant meals to strengthen the public charities fund. The trend of tax receipts as a whole tended to keep up until June 1931, the increases in the gasoline tax and succession duties being sufficient to offset the declines that were already occurring in other taxes, as a result of the depression.

The effect of the growth of direct taxation yields in the boom period (by almost 157% between 1926 and 1931 fiscal years) was to reduce still further the proportion of total revenue that came from the federal subsidy and from the domain. In 1925 these together had yielded 33% of total revenue, but by June 1931 they produced only 18%. The decline in their proportion was due, not only to the rising yields of other sources, but also to the decrease in domain revenues from $6.5 million in 1925 to $5.4 million in 1930. The decline in domain revenues resulted principally from the contraction after 1927 in payments by parties exploiting the forests.(17) Apart from domain revenues, all others increased from 1925 to 1930, and by then direct taxes and liquor "profits" produced 61% of the total revenues.

The extent and the severity of the depression affected the different revenue items at different times and to different extents. As already indicated, the revenues from public domain, connected as they were with the forestry and pulp and paper industries, declined from 1927 onwards, their level in 1930 being

(17) The contraction of the lumber trade, followed by the collapse of the pulp and paper industry, resulted in a fall in the timber cut on Crown lands from 1.6 billion feet in 1927 to 900 million in 1931.

17% below that of 1925. In other sources, the downtrend was less marked at this stage. Motor vehicle licences and gasoline taxes combined, showed a smaller rate of increase in 1929 than in 1928, but their total yield was also still rising in 1929. The same was true of the liquor sales. Accordingly during the year ending June 30, 1931, in all revenue items, except public domain, the total yield was above that of 1925, the main increases being in succession duties and gasoline taxes. However the change in the rates of increase after 1928 pointed to the situation that was emerging, and in 1931 the government took steps to try to prop revenues. The gasoline tax was raised from 5 cents to 6 cents, the amusement and meal taxes were raised to aid public charities, and the corporation tax was altered in February 1932, to be effective in 1933, a profits tax of 1½% being imposed by this measure. Nevertheless total revenues declined till June 1934, the main revenues (except motor licences and amusement taxes) being at their lowest point of yield in that year. (The two exceptions touched their low points in the previous years.)

Revenues from direct taxation decreased from $17.3 million in 1930 to $14.4 million in 1933, but expanded in the recovery, and with the new taxes and rates, to $18.8 million in 1936.

In the recovery period from 1933 to 1936, the increase in revenue has been produced mainly by corporation taxes (including the new profits tax) and succession duties. Total taxes accounted for 45% of the increase. Liquor and

public domain accounted for 34% between them,[18] and the remainder of the increase came from other items, chiefly licences, permits and fees. The large increase in corporation taxes was aided by the new rate of profits tax (2½%) imposed in 1935, and the increase in succession duties by the important rate alterations in the same year. The rate of expansion of domain revenue after 1933 reflected the improvement in the demand for newsprint and for sawn lumber, as well as the higher stumpage dues imposed in 1934. The larger liquor profits reflected the improved purchasing power in the recovery period, and also the effect of the special stamp duty imposed in 1933 on sales of bottled alcohol or spirits. The rapid growth of metal mining in the Province showed itself in the increased yield from the level on the profits of mining companies, the levy rising from $90,000 in 1925 to $1 million in 1936. If mining activity continues to expand, government revenue from this comparatively new field of production would become a relatively important item among the corporation taxes.

The provincial revenue system in Quebec still neglects certain taxes adopted by some other provinces, in particular taxes on income, on real and personal property, and on retail

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(18) Non-tax Revenues
$000

	Fiscal years ending June 30th		
	1931	1934	1937
Liquor Control	9,180	2,367	6,312
Public Domain	5,411	2,897	5,328
Motor Licences	5,410	5,205	6,484
Federal Subsidy	2,256	2,592	2,592
Other	3,589	3,243	3,985
Total Non-tax	25,846	16,304	24,701
Total Revenues	43,111	30,722	43,489

sales. But these taxes have been used by municipalities in Quebec, particularly in Montreal. The extent of urbanization in Quebec, and the degree to which these municipalities meet necessary services, has involved a high debt level for municipalities. In 1936, the gross funded debt of Quebec municipalities amounted to $517 million, as against $246 million in 1926, the increase having been due mainly to the effects of the depression. This condition may affect the provincial government both in expenditure and revenues. The exhaustion of municipal financial resources might necessitate grants to municipalities. The fact that municipalities have to use their revenue possibilities so far as possible, in turn affects the revenue possibilities of the provincial government.

SUMMARY

1. The outstanding feature of the Quebec financial position at present is the transition from a negative to a positive developmental policy in expenditures, particularly capital works. The main emphasis in expenditure tends to be towards highway improvement, and towards works and methods that will increase the utilization of the provincial resources. These measures give expression to fundamental aims concerning the proper balance of population between town and country, and concerning the proper extension of certain types of welfare services.

2. The transition is more evident in the expenditure than in the tax system. This is partly attributable, however, to the incidence of the depression which increased the urgency of relief and added emergency responsibilities to the provincial government. Relief forms almost half the recent debt growth. The remainder of the debt went mainly to developmental works, and the existent emphasis on positive policies is likely to add to the "active assets" and debts of the Province.

3. Since 1930 Quebec's ability to meet emergency expenditures, and to undertake more vigorous public programmes, was largely determined by her previous financial policy, during the pursuit of which spending was kept in line with revenues, and new debt growth was minimized. This history strengthened Quebec's credit, and gave also some reserve of revenue-raising powers. Recently, however, the growth of expenditure has tended to outrun the use of the revenue powers, the tax base being still comparatively narrow. Even in 1936 the bulk of the taxation came from the long-established corporation taxes and succession duties, and the comparatively new gasoline tax. Considering the debt levels and tax systems of other Canadian provinces, Quebec appears still to have some latent reserves of credit and taxation with which to pursue her new policies. However, a speedy rise in debt or taxation to a given level tends to carry disadvantages that would be absent in a more gradual increase.

Financial Position of Ontario

In the 19th century, both before and after Confederation, the province and the municipalities in Ontario had directed some efforts at developing and expanding the economy, in particular by assistance to the building of railways. But after Confederation, the main jobs of development - the extension of the frontier, and the further expansion of Canadian transportation, - were mainly Dominion undertakings, the completion of which, it was expected, would quadruple the trade of the city of Toronto, as Tilley said in the 1873 Budget Speech. The decision to undertake the national tariff policy in 1879 also seemed likely to encourage private enterprise, and accordingly the Ontario government gave most of its attention at this time to the provision of the current services of government - justice, education and welfare - rather than to capital works. Quebec's venture into government ownership - the operation of the Quebec, Montreal and Ottawa railway - seemed to increase Ontario's traditional dislike of that form of government activity, and this example, combined with the fact that railway mileage in Ontario was continually expanding, seemed to suggest the unwisdom of Ontario's undertaking further provision of capital equipment of this sort. Although towns were growing, and some diversification of manufactures gave promise of further urbanization, the costs of municipal works - roadways, waterworks, lighting, transport - reflected themselves in the municipal rather than in the provincial debt picture. Ontario's expenditures on developmental projects were thus comparatively modest in the last quarter of the 19th century. Small sums were spent on agriculture, this industry being in process of readjustment as a consequence of the opening of the American west, which increased wheat supplies, and as a result of the growth of small urban centres in Ontario, which provided markets for mixed farming. Small amounts were spent also on colonization roads,

but significant highway expenditures did not begin until the passing of the Highway Improvement Act of 1901. The main concerns of the provincial government were education, public charities, the liquor traffic, and court and law reform.

In the last quarter of the century current expenditures increased five-fold. This was partly due to the increase in population, which rose from 1.6 million in 1870 to 2.2 million in 1900, and partly to the growth and the improvement of governmental services. In education, expenditures had amounted to only $315,000 in 1870, but had reached $1.1 million by the turn of the century. In the interim the number of children had increased, a school age limit had been set, and new standards for teaching schoolrooms, secondary school provision and grants for higher learning, had combined to raise costs. Public welfare costs rose by about the same amount in the last quarter of the century, due again to the increase of population, to improved methods of sanitation and hospitalization, and to the differential treatment of mental and other diseases. The increasing complexity of the economy involved steady increases in the costs of administration and in the specialization of administrative departments.

Growing expenditures had tended to outrun provincial revenues, despite increased returns from the public domain. Timber export was an important phase of the economic life, especially the export to the growing New York and Chicago area, and the concomitant growth of large-scale saw-mill development in the province encouraged the government to display some ingenuity in devising new levies on timber. Towards the close of the 19th century new timber licence conditions were imposed, and the export of logs and pulpwood was discouraged in favour of the manufacture of lumber and pulp. But the doubling of domain revenues and the increase of Dominion subsidy in 1884 were not

sufficient to counterbalance growing expenditure needs and in 1892 direct taxation was imposed in the form of succession duties. In 1892 the Act applied only to property in Ontario, but in 1895 it was made applicable to all property held by residents. But further increases in expenditures necessitated the raising of additional revenues and in 1899 the Supplementary Revenue Act was passed, taxing banks, insurance, loan, trust, railway, telegraph, telephone, gas, electric, express and sleeping car companies. By then had appeared the first evidences of the trade improvement leading to the long boom that lasted until the War. In the early 20th century, as the Canadian west was opening and as America was indicating further economic expansion, the Province of Ontario took a more positive position with respect to development. Expansion of Northern Ontario, and connection of that region with Toronto and the south, seemed necessary to prevent the trade of the Temiskaming country being diverted to Montreal. In addition, it seemed desirable to have a railway into Northern Ontario that would connect with lines penetrating the new and promising prairies, and perhaps later construct a branch of its own to James Bay and a northern seaport. At the turn of the century this aim seemed to be settled and the main question was whether the government should subsidize a private line, or construct a line of its own in order to exercise control over rates and to expedite development. The latter course was decided upon, and in 1902 the Temiskaming and Northern Ontario Railway Act was passed providing for the construction of a line from North Bay to a point on Lake Temiskaming near Haileybury and New Liskeard.

The second developmental policy initiated in this first decade of the 20th century, which concerned the growing hydro-electric industry, appeared somewhat less positive in its inception. In the budget speech of 1910, several years after the scheme had been in operation, the Provincial Treasury was

able to emphasize the fact that the Province was not manufacturing power: it was simply regulating the transmission of power. Nevertheless, the conditions existing at the initial formulation of the scheme suggest that a somewhat more positive scheme of government control was envisaged. The asset of the Niagara Falls was an obvious one and American capital, besides developing power on the American side, was beginning to be invested on the Canadian side. Patriotic considerations, and the prospect of cheap power in a region requiring imported fuel, combined to motivate the provincial Acts of 1906 and 1907. In the beginning the Hydro Commission purchased power from privately-owned generating plants, and attended to the establishment of a comprehensive system of power supply to a large territory through control of power distribution. In 1908 the Commission began operations, acting on behalf of the municipalities that had contracted with it for a supply of electricity, and it entered into a contract with the Ontario Power Company for the purchase of electricity. The Commission did not engage in the generation of power until 1917. But although the Hydro policy in the pre-war period seemed the less positive of the new governmental projects of development, it was destined to become a unique organization in the field of economic effort. "In years to come it will be the tool-case of a rational state socialism", says Mr. C.R. Fay. But in the pre-war period this prophecy would have had nothing to support it.

Up to the War the railway undertaking was more important from the point of view of provincial liabilities. And the opening of the mining areas around Cobalt and the newly found Porcupine district already seemed to justify this provincial railway venture. These areas seemed likely to expand and to counterbalance the loss of traffic that would come when the work of transporting the supplies for the new National Transcontinental Railway ceased. By 1916 the Hydro was still

a relatively small enterprise, while in that year the railway was able to pay one million dollars into the provincial treasury. (A payment of this amount, however, did not become an annual custom.) But the Hydro had already expanded from serving 10 municipalities in 1910 to 191 in 1916 and the war boom and the concomitant demand for increased power, especially in industrial regions, was urgent. Given this demand, and given the forceful leadership that characterized the Hydro Commission, the probability of a change in policy from mere distribution to distribution and production, was a considerable one, and the change was initiated by the acquisition in 1917 of the plant and transmission lines of the Ontario Power Company. In the next few years, with the emergence of the war and post-war booms and the need for enlarged power, the Commission acquired further enterprises (e.g. Toronto Power Company), and also embarked on pioneer construction (e.g. Queenston-Chippewa development). No further notable acquisitions of private concerns occurred until 1930 but the activities of the Commission in the war years indicated that the logical conclusion of its policy would be sufficient control over the Ontario power industry to allow sale of power in both rural and urban areas at rates satisfactory to the community as a whole.

Up to the War, therefore, the Province of Ontario was following a double-headed policy of development. On the one side, like the Dominion government and like some other provinces, it was encouraging a further extension of its frontier by a railway expansion calculated to open new areas and to develop new supplies of resources. On the other side, like those provinces that were encouraging a more intensive economic growth (e.g. telephones, agricultural aid, etc.) Ontario was heralding a new form of intensive development calculated to cheapen power, and aiming rather at providing a new power method for utilizing resources than at the discovery of new sources of supply which

was the objective of most pre-war development in Canada. The Ontario Hydro plan, with its municipal attachment, was directed at reducing costs of power, and both directly and indirectly was likely to stimulate the production of new goods and services, and to encourage more efficient methods of industrial production - in short to encourage development of an intensive rather than an extensive kind.

By 1913, the Ontario balance sheet showed an outstanding debt of $41.5 million. The capital investment in the Temiskaming and Northern Ontario Railway was at that time $19.7 million, and the government investment in Hydro only $6 million. A guarantee of $7.9 million was outstanding in respect of the Canadian Northern Pacific Railway. Active assets covered the bulk of the remaining debt, cash on hand amounting to $2.4 million and advances to $3 million. Of the latter indirect liabilities, $900,000 were for the Niagara Parks Commission and approximately the same amount for the University of Toronto.

At that time, Ontario revealed a condition that has been unique in Canadian public finance: the interest received by the province exceeded the debt charges, a position partly due to the receipt of special interest from the Dominion subsidy on the government railway. But that special grant, which raised the interest received in 1913, must not dim the fact that Ontario was already pursuing a policy uncommon in Canada - the gathering of a profitable enterprise within state control. Generally, governments found it necessary to engage in enterprises on which the margin of profit, if any, was small. In Ontario, however, the Hydro undertaking, even by 1921, was able to yield sufficient interest to make the Province's net debt charges, as a percentage of expenditure, low as compared with other provinces (9.5% as against the general level of 15.7%).

In the pre-war period also the provincial government attended to intensive development in its ordinary expenditures. The opening of the west and the expansion of western agriculture necessitated some readjustment within the agricultural

economy of Ontario. The Canadian pre-war boom (1896-1913) brought new agricultural supplies into competition with the Ontario output, while the urban and manufacturing expansion within Ontario itself also affected local agriculture. The net effect was a definite trend towards mixed farming and certain specializations in Ontario agriculture. To some extent conditions arising out of the War interfered with this agricultural adaptation. There arose profitable markets in Europe for Ontario farm produce, so that export trade was stimulated. But the main trend in the early 20th century was the adaptation of Ontario agriculture to new and growing urban needs. This adaptation was aided by the provincial administration. The activities of the Ontario Agricultural College were extended and the government assisted agricultural and dairy schools, experimental and demonstrative farms, fairs, the work of rural institutes and the work of soil survey. The appointment of paid agricultural representatives was another manifestation of the government's desire to encourage scientific methods in this industry. Under this heading should be added the special grants made for the development of Northern Ontario after 1912.

In another direction also, the Province of Ontario adopted a more positive policy that had long-term ends in mind, mainly the expansion of the educational system. It was in the first decade of the 20th century that the present system of provincial grants for schools was established, although subsequent modifications have been many. Before that time grants had been made on the basis of population of districts and average attendance at schools within the districts. But a desire to improve education, coupled with a realization that in the pre-war boom teachers' salaries were not attractive and that Ontario teachers were migrating westwards, encouraged a change in provincial policy. It was felt that grants would have to be made to improve standards and to ensure that inequality of wealth between

different school districts did not impede educational progress in the less wealthy areas. These principles along with others that crept in later (e.g. the improvement of equipment, the attempt to raise teachers' standards by making grants on the basis of their qualifications) were restated in the legislation of 1931 which established five factors as the determinants of legislative grants. At the outbreak of War, however, education was the most significant item in the general expenditures of the Province. In 1913 the expenditures were as follows:

	1913
	$000
Education	2,653
Domain	2,510
Welfare	1,522
Net Debt	122 (cr.)
Government	1,151
Justice	910
Highways	565
Agriculture	393
Legislature	370
Other	572
Total	10,524

In 1913, the domain expenditure was only $881,000 but $1,629,000 was spent on lands and forests and public works. This item has been added to the domain expenditure. Following education, welfare was the second important item of expenditure, most of this expenditure going to provincial institutions, of which the mental institutions were the most important. Education, welfare, and general government (including legislation and justice) accounted for 63% of the expenditures, the remainder of the expenditure going to debt, highways, agriculture, etc. In 1913, therefore, despite the developmental policies that had been instituted, the pattern of the expenditure system was a simple one. But the introduction of more vigorous policies indicated that the province was entering a period of transition from a simple to a complicated budget pattern. Some measure of the changes that were beginning or imminent may be got by

contrasting the 1913 and the 1921 expenditures. They rose from $11 million to $22 million in the period. Interest receipts exceeded gross debt charges by $122,000 in 1913; in 1921 net debt charges were $2,131,000.

In 1913, however, both the revenue and the expenditure systems were fairly simple. The revenue system still depended greatly on the subsidy and on the domain revenues. The revenues were:-

	1913 $000
Domain	2,887
Subsidy	2,396
Taxes	2,083
Liquor Control	902
Licences	866
Others	235
Total Revenue	9,369

Already, however, taxes were beginning to prove productive. Succession duties began to reflect the rise in private incomes that followed economic expansion, and corporation taxes were also becoming more important as manufactures grew and as banks, insurance and other taxable companies expanded to meet the new economic conditions. In 1905 succession duty rates and corporation taxes had been revised upward.

But although the domain revenues and the subsidy were still the outstanding revenue items in Ontario in 1913, the transition of the revenue system to a broader basis was also well advanced. The domain and the subsidy which had formerly produced 80% of the revenue yielded less than 60% in 1913. The subsidy, despite the 1907 readjustment which was not unfavourable to Ontario, was too stable to prove significant in the face of growing needs, while the public domain revenues were also likely to have definite limits, even if the decline in the saw-mill industry were compensated by the growth of a new pulp industry. In view of these conditions, and in view of the dynamic nature

of the budget, it was likely that an increasing portion of the revenues would have to be sought from taxes that would be expansive under the dynamic forces of industrial growth and large-scale enterprise.

The war experience seemed to act as a forcing-ground for the developmental policies that had been already seeded. Of the rapid growths that took place the most significant was in the Hydro scheme. But the creation of the Department of Public Highways in 1915, the establishment of the Toronto-Hamilton Highway Commission, the advancement of housing and agricultural projects, the expansion of education and the new undertakings in public welfare, all served to effect a rapid change in the budgetary picture between 1913 and 1921. This rapid rate of expansion of governmental activities continued up to the depression after 1929. These changes reflected themselves in an extremely rapid growth of direct and also indirect liabilities. The main indirect liability was the guarantee of bonds of the Hydro Commission, this one item accounting for 81% of the indirect liabilities by 1936, the remainder being mainly guarantees of railway bonds, and small obligations of universities, park commissions and municipalities. The guaranteed bonds are large in amount, being more than one-fifth of the amount of the direct liabilities, but their significance lies in the fact that they cover mainly Hydro operations.

In order to see the continuity of the development of certain provincial programmes, it has been thought worth-while to give a brief outline of the more important provincial investments as they developed from the war period up to 1936.

The government investment in Hydro rose from $6 million in 1913 to $113.7 million in 1921, (including guarantees of $12 million). By 1929 the government investment had risen from its 1921 level of $113.7 million to $203.5 million, and by 1936 the investment was $254.4 million, including guarantees

of $112.8 million. (Since 1934, new capital borrowings of the Hydro Commission or issues from refunding have been effected through the obligations of the Commission under provincial guarantee, rather than through direct provincial bonds.)

As power shortage threatened the Hydro Commission in the early phase of the war boom, and as it had already acquired several years' experience in the power business, the Commission entered the generating side of power production by the acquisition of the Ontario Power Company's plant at Niagara, the undertaking of the Queenston-Chippewa development and the purchase of the Toronto Power Company's plant and transmission lines in 1920. These were the initial outstanding schemes of power generation, although subsequent purchases of a smaller sort furthered this movement (e.g. acquisition of Georgian Bay System plants).

The more recent Hydro developments were probably hastened by the 1925-9 boom. In response to increasing demand, the Commission tried to ensure adequate power, especially in Southern Ontario. There was and still is undeveloped power on the St.Lawrence river. But the development of power from the river is connected with navigation development and the international questions to which these considerations gave rise have involved extended negotiations. The Commission had. therefore, to revert to an alternative source of supply through long-term contracts with four Quebec companies. These contracts are still in force though amended. The Commission acquired in 1930 the Dominion Power and Transmission Company at Hamilton, and in 1933 the Ontario Power Service Corporation at Abitibi Canyon. Further extensions were made in the Thunder Bay system. In the past few years there has been some extension of rural lines by legislative grants - the only monies provided by the province at the general cost of the taxpayer for the construction of Hydro plant.

It is possible that increased demands may be met in the future by new power developments particularly on the St, Lawrence and Upper Ottawa regions, and any such expansion would involve a considerable addition to the capital structure of the Commission. In that event, ownership of the Commission's assets will tend to rest more and more with the people of the province as a whole, rather than the municipalities, which also have an equity in the system.

This state enterprise, owned by province and municipalities, is unique in its history, organization and policy. Its history has been the emergence of a state enterprise that pushed back from distribution to production of power by the acquisition of private firms, by trustification, and by its own capitalistic expansions. Its organization in the form of a Commission that built a valuable and self sustaining asset with provincial and municipal funds, and used these funds to serve large-scale technique and large-scale control, is perhaps a unique example of the apt reconciling of a socialized financial unit with capitalistic technical, managerial, and marketing units. Its policy of maintaining reasonably low rates and of providing reserves for depreciation along with reserves for retirement of the capital debt standing against the plants is also unique. The success of the venture in which potentialities of additional earnings are great, led other provinces to attempt similar power development. But the success of the Ontario scheme was due to a combination of factors that cannot often occur - forceful and independent management in the formative period, the existence of a natural asset of Niagara Falls, and the presence of an extensive demand for power for manufactures and for households.

The second important provincial investment to be discussed is highways. By 1936, the provincial investment in highways, including relief works on highways, was $254 million the largest single balance sheet item, or 32% of the outstanding

debt. Road expenditures had tended to rise with the economic expansion of the pre-war boom, the province having passed the Highway Improvement Act of 1901 to assist the counties in road construction, and having given attention to colonization roads and to northern road development in areas that lacked county organization. The main impetus to road expansion however coincided with the intensive economic development that took place in the war boom. The newly instituted Department of Public Highways (1918) and the new experimental road commission that undertook the construction of the Toronto-Hamilton road, were confronted not only with the problems of road building but with those of regulation of the new form of transportation.

An important phase of the highway question that was reflected in other provincial concerns (e.g. Hydro, education, welfare etc.) was the problem of ensuring a fairly comparable rate of development in different areas of the province. In 1916 the provincial grant for county road construction was increased from 33-1/3% to 40% and grants of 20% in aid of maintenance were initiated. In 1917 certain county roads were designated provincial roads and on these the provincial government provided 60% of the construction and maintenance. In 1918 the maintenance grant on the county roads was raised from 20% to 40%. In 1925 the county road system was revised. For township and Indian Reserve roads, provincial assistance was also given, 20% for general work and 50% for superintendence after 1920. In 1925 the grants were increased to 30% and 50% respectively, in 1930 to 40% and 50% respectively and in 1937 to 50% for all approved highway expenditure.

At present the provincial government's road expenditures are as follows:

(1) The province bears the full cost of King's Highways.

(2) On county highways, the provincial government contributes 50% of the amount of the county's expenditure on improvements, as well as the ordinary maintenance grant.

(3) In townships the province pays 40% of the expenditure on roads and 50% of the expenditure on supervision. The former percentage may be as high as 80% if the Minister deems that necessary.

(4) In cities, the province joins with the county in assisting suburban roads, giving 50% of the cost, the city and county dividing the remainder between them.

Since the beginning of the 20th century, the province has contributed almost two-thirds (60%) of the total road expenditures, but recently the provincial proportion has tended to rise according to the extension of King's Highways, and the increase of grants to counties and townships. These circumstances indicate that the future highway expenditure of the provincial government is likely to increase as a proportion of total highway expenditure, and since at the same time total highway expenditure is also likely to rise, provincial expenditures on both capital and current account are likely to reflect this trend. The grounds for the expectation that total highway development is likely to proceed apace are indicated in the statements of the Provincial Treasurer in the 1938 budget speech. Road traffic on the Windsor-Quebec route has already reached proportions that suggest the need for larger arterial roads.

Highways expenditures in Ontario have been determined mainly by the geographical location of the province and by its industrial characteristics. The province required an intensive expansion of highways within its urbanized areas to link them, and to provide a route to industrial America. At the same time, the nature of the province and the advancing of its northern

frontier required an extensive system of roads. Accordingly since the War, while the main highways of Southern Ontario have been extended with some rapidity, it is important to note that the proportion of total highway outlay spent in Northern Ontario has tended to increase steadily. The proportion of government road investment in the North has increased from 13% of the total road investment in 1921 to 22% in 1936.

Ontario's road development since the War, being both cause and effect of industrial progress, has had developmental effects in the province not unlike those produced for Canada as a whole by the railway expansion in the pre-war period, except that Ontario's road building seldom appeared to be creating unused capacity, or capacity large enough to serve some conjectural future demand. Road improvement has been accomplished in response to existent demands for linking urban areas, and as such it has widened the Ontario internal market, has lowered the costs of competitive transport, and affected the volume of the tourist trade. In this way it has affected the income of households and firms within the province. Provincial finances have also been affected by the increases in motor licences and gasoline tax revenues which, together, cover the province's current expenditures on maintenance and interest on the highway investment. In Ontario, however, it is noteworthy that while the municipalities are required to provide for the retirement of their highway debts, no such provision is made by the province itself. Provincial highway debt shows a marked tendency to rise and highway investment becomes increasingly dominant in the direct liabilities of the province.

As already indicated the Hydro and highways accounted for about two-thirds of Ontario's outstanding debt in 1936. The remainder was attributable to the railway, to lands and buildings, to agricultural loans, to the accumulation of deficits, to the capitalization of direct relief, to the bonus on rural power transmission, and to numerous lesser items.

At the outbreak of the War, the Temiskaming and Northern Ontario Railway was the major commitment of the province, accounting for over 45% of the total liabilities of the province at that time. The government made capital expenditures on this railroad in the hope that they would be recovered, not necessarily from the railroad itself but, like the highway investment, from other sources provided by the opening of the new frontier. There was thus an indeterminate relationship between the government investments and subsequent government revenues. In this case it was true that the construction of the line, and the rate policy followed, hastened the exploitation of the resources of the region, particularly in minerals and pulp, but it is equally true that speedy exploitation of resources of this sort may prove to have long-run costs that tend to lie on the government as such regions suffer exhaustion of their resources.

In the post-war period, the Temiskaming and Northern Ontario was expanded with branches into the growing mining areas, and with an extension as far as James Bay. The construction of branches into the mineral properties soon justified itself from the Railway's point of view, especially in the depression years after 1929 when mineral expansion compensated in part for the decline in the newsprint freight. While the northward construction could, for part of the way, assist the development of mineral, power and lumber resources, the recent (1932) extension to James Bay has not yet been justified. Up to the present the railway as a whole has called for an investment of $30 million by the provincial government plus $11 million in guaranteed bonds and bank loans, in all some 5% of the total direct and indirect liabilities of the Ontario government. The line has not been directly self-sustaining; deficits were at their lowest in the boom (1925-9) but increased again in the depression. Up to 1937 the investment cost the province over $37 million in interest. Since over $16 million

was received in revenue from the line, the net money cost to the province may be measured at $21 million. It has to be remembered however, that the province received a lump sum payment from the Dominion government as a subsidy for the building of the line. In 1913 the province received a subsidy of $2.1 million. The revenues that accrued indirectly from the existence of the line have been considerable, but their precise relationship to the cost of the line itself is indeterminate. The development of the northern country, the direct revenues received from mines and lumbering activities, as well as the revenues raised from dividend receivers are, however, of prime importance to the government of Ontario.

After this outline of the history of the major government undertakings from the War onwards, it is necessary to consider the financial conditions during these years. The War and the post-war booms involved a considerable expansion of income to the households and firms of Ontario, agriculture, lumber, minerals, and manufactures all having expanded, and there was likewise an expansion of services, not the least important of which was the growth of financial houses, and the centralization of large-scale undertakings in Ontario. The counterpart to this expansion of private enterprise was to be found in the expansion of government enterprise. The growth of the Hydro undertaking during this period has already been discussed. By 1921, the outstanding debt of the province was $219 million. The increase over 1913 is shown in the following table.

	1913 $000	1921 $000	Increase $000
Active Assets	5,502	35,319	29,817
Hydro	6,023	113,674	107,651
T. & N.O.Rly.	19,696	23,600	3,904
Canadian Northern Ontario Railway (a)	7,860	(a)	-7,860
Public Works	-	51,987	51,987
Advances	56	6,280	6,224
Surplus (-) or deficit (+)	+ 2,399	- 11,906	-14,305
Outstanding Debt	41,536	218,954	177,418

(a) Later assumed by the Canadian National Railway Company.

Of the 177 million dollar debt increase, the Hydro was the outstanding cause. The increase in public works (on capital account) was not shown in the 1913 accounts but by 1921 highways had accounted for $26 million of the subsequent increase, and buildings for $26 million. The increase in active assets was due mainly to an increase in cash, and to a $6 million dollar advance to municipalities. The increase in advances (on which partial or no interest has been paid) went to municipalities ($3 million) and to the Sandwich Windsor and Amherstburg Railway ($2.5 million).

By 1921 the revenues and expenditures of the province also revealed the growing complexity of the Ontario economy. Net debt charges, education, welfare and government formed over 70% of total expenditures.

	1913 $000	1921 $000	Increase $000	Decrease $000
Net Debt Charges	122(Cr)	2,131	2,253	
Education	2,653	7,021	4,368	
Government	1,151	3,490	2,339	
Welfare	1,522	3,514	1,992	
Justice	910	1,624	714	
Highways	565	1,173	608	
Agriculture	393	835	442	
Other	572	892	320	
Legislation	370	388	18	
Domain	2,510	1,366		1,144
Total Expenditure	10,524	22,434	11,910	

It will be noted that the domain expenditure is recorded as having fallen. Forest and other services increased during the War, but the 1913 figure had included within it a sum spent on public works and on forests.

The rise in the net debt charge was due to the debt growth which was discussed above. The rise in education expenses was due largely to the increased grants to schools and universities, the rise in government costs to increased personnel and expansion of government services, and the rise in welfare to the expansion of institutions (mental, tuberculosis, deaf and dumb, and homes

for infirm), the new level of grants to hospitals, and the new labour department. Mothers' allowances were only beginning in 1921.

The expenditure system of the province was therefore indicating the growing complexity of the government service, as economic expansion induced the government to undertake new capital works, and as the demands for improved education and welfare services raised the levels of these items. The revenue system indicated also the growing diversity of the economy and the increasing dependence on taxation for revenue.

	1913 $000	1921 $000	Increase $000	Decrease
Dominion Subsidy	2,396	2,396	-	-
Taxes	2,083	9,824	7,741	
Licences	866	4,313	3,447	
Domain	2,887	3,725	838	
Fines	37	672	635	
Sales	18	332	314	
Refunds	69	191	122	
Liquor	902	349	-	553
Other	111	105		6
Total Revenue	9,369	21,907	12,538	

Almost two-thirds of the increase in revenue came from taxes. Among the tax increases the most significant was in succession duties, and after that in corporation taxes, the race track companies yielding the largest single company increase, but all companies revealed the effects of the economic expansion, and the changed tax rates. New amusement taxes also aided considerably the rise in revenues. The rise in licences came mainly from increased ownership of motor vehicles, and the increase in domain from forest royalties, forest fire tax, and fur licences and royalties. The increase in fines accrued from the Ontario Temperance Act, and the fall in the liquor licences resulted also from the change in the liquor laws. By 1921 taxation was yielding 45% of the revenue and licences 20%. The subsidy and the domain, the

original "Confederation" revenues, together yielded only 28%.

The financial history of the years up to 1929 was mainly a reinforcing of the trends of capital works, expenditure and taxation that had emerged in the War and post-war booms. There was some slight change of emphasis, however, in that the rate of increase of expenditures on highways, and on loans that paid partial (or no) interest, was greater than the rate of increase of investment in interest bearing projects. Among the advances which have borne little or no interest, the most important were those to the Agricultural Development Board established in the post-war depression, when Ontario agriculture was trying to readjust itself to more normal conditions after the war boom. Theoretically, the funds for this farm credit were to be raised through the new Ontario Savings Offices, and the province was to advance these as loans to the Development Board in return for debentures carrying a slightly higher rate of interest than that paid by the province to the Savings Offices. The Board placed the loans with farmers at 5½% for an amount to be not more than 50% of the valuation. In time, however, the financial relation of the agricultural Board and the Savings Office became less apparent, particularly in the depression after 1929 when the demand for agricultural loans increased at the time that savings deposits were being withdrawn and reduced. In these conditions the province's interest in the Loan Board increased rapidly. The loans to the Board doubled between 1928 and 1936, and since the Board's payment of interest to the province fell behind, the provincial equity in the Board more than doubled over the period and now amounts to about 7.5% of the direct liabilities of the province. The agricultural depression affected the soundness of many of the mortgage loans made by the Board, and despite adjustments more than half the accounts were in arrears in 1936. The unsatisfactory position of these assets is evident from the opinion expressed by the Provincial

Treasurer in the 1938 Budget Speech to the effect that 50% of the loans are in such a position that even if all the outstanding interest on them were forgiven and some discount on principal allowed, they still could not be liquidated because the amount originally loaned exceeded the real loanable value of the property. The effect of the Agricultural Development Board on Ontario's debt structure is one measure of the effect of the post-war agricultural revolution on the economy of Ontario.

In the post-war period, the Agricultural Advances, along with the much larger extension of Hydro investment, and the still larger capital expenditures involved by the transport revolution, dominated Ontario's debt increases up to the depression (after 1929). The change in the balance sheet in the post-war period was:-

	1921	1930 ($ millions)	Increase
Active Assets	35.3	38.2	2.9
Utilities	137.3	271.6	134.3
Public Works	52.0	187.4	135.4
Advances	6.3	39.7	33.4
Deficit	-11.9	12.3	24.2
Other Expenditures capitalized		4.6	4.6
	219.0	553.8	334.8
Less Sinking Fund Reserve		1.1	1.1
Outstanding debt	219.0	552.7	333.7

During this period the investment in public works slightly exceeded that on the utilities. Of the $135 million increase in public works, the new road activities accounted for $120 million, and public buildings for $15 million. In the utilities, $121.6 million of the $134.3 million increase was attributable to the power commission, and $12.6 million to the railway extension (i.e. branch lines and main line from Cochrane to Island Falls and on to Coral Rapids). Of the 33 million dollar increase in advances, $30 million went to the Agricultural Development Board. Although there was little change in the total active assets between 1921 and 1930, there

was considerable change in the items making up the total. There were increases in advances to municipalities, in the liquor control board surplus, and in inventories, etc. The post-war depression, and the growing charges for debt (i.e. apart from Hydro) for welfare, education, maintenance of the rapidly growing highways, had all served to increase the deficits on current account. From 1927 to 1929 however, surpluses emerged.

The rise in current expenditure was fairly steady between 1921 and 1930, and it affected all items of expenditure. The following table arranges the services in the order of their increase in this period.

	1921 $000	1930 $000	Increase $000
Net Debt Charges	2,131	9,659	7,528
Welfare	3,514	12,851	9,337
Education	7,021	12,895	5,874
Highways	1,173	6,836	5,663
Domain	1,366	4,595	3,229
Justice	1,624	3,128	1,504
Government	3,490	4,328	838
Legislation	388	1,024	636
Agriculture	835	1,357	522
Other	892	2,756	1,864
Total Expenditures	22,434	59,429	36,995

The growth of debt charges for public works and other purposes was becoming a significant item. In 1921, Ontario's net debt charges were only 9.5% of annual expenditure, while the provinces as a whole spent 15.7% of their total on this item. But in the post-war period, with the expansion of highways, etc. Ontario's percentage rose towards the general average, and by 1930, Ontario was spending 16.3% of her total expenditure on net debt charges, as against the 15.7% for the provinces as a whole. Ontario by 1930 spent 59.6% of the total expenditures on net debt charges, education and welfare.

Education had always been the outstanding charge in Ontario, but by 1930 welfare expenditures had grown rapidly and were about to overtake education. The significant jump did not occur until 1930, old age pensions being the important contributor to the latter rise. Before that time the growing factors under this heading were public institutions, particularly mental institutions, the introduction of mothers' allowances in 1920 and the gradual enlargement of hospital grants. The growth in pure public health services was modest by comparison. The effect on the budget of the introduction of new items like the mothers' allowance and old age pensions is evident. The growth of institutional and hospital grants is, however, worthy of some notice. In Ontario, the direct administration of health devolves largely upon the municipalities, the revenue being provided mainly by fees and municipal grants, a part coming also from donations and provincial grants. Mental institutions on the other hand are mainly a provincial responsibility, the municipal contribution to these being only a small part of their total cost. The provincial grant to general hospitals expanded as the costs of hospitalization increased, and in the last decade the proportion of the total general hospital income derived from the province increased from 8.6% in 1927 to 11.3% in 1936. In 1937, however, the provincial grant was reduced. In the homes for incurables the proportion of income derived from the province also tended to rise until the reduction of the grant in 1937 reduced the proportion paid by the province from 23% to 20%. In sanatoria for consumptives the provincial responsibility has also tended to increase. The main provincial expenditure is, however, on mental hospitals and the total expenditure has risen steadily, the province providing almost 70% of the income of these institutions. Apart, therefore, from the recent relief payments made under the head of welfare and apart from the effects of the depression in adding to mothers' allowances

and old age pension payments, the rise in hospital grants, the high level of expenditure on institutions, and the tendency for free public health services to increase have contributed to a new trend of welfare services. Although certain beneficiaries from mothers' allowances and old age pensions might appear on relief rolls if these services were absent, it is noteworthy that actuarial calculations indicate that old age pension costs are likely to become increasingly significant in the next decade. Certain other services (e.g. preventable disease control, tuberculosis etc.) will likely reflect the trend of changing public opinion on these matters. To the extent that relief costs fall, the government will find it easier to meet the growing public welfare costs on the basis of its present budgetary position.

Before the War, education which absorbed about one-quarter of the total disbursement, was the outstanding expenditure of the provincial government. By the end of the boom, (1930) it accounted for almost 22%, but the reduction in education costs and the expansion of other services, leaves education now as the third item in the budget, taking about 14% of expenditure. The reduction in the provincial costs of education have been marked since 1931 (22% between 1931 and 1936): since teachers' salaries formed almost three-quarters of the total education costs in Ontario it is clear that the reduction has been due mainly to the fall in salaries. The rise in Ontario's total education cost since the beginning of the century has been associated with the increase in the number of children, and with the improvement in the standards of education. This has reflected itself in the increasing relative importance of secondary and vocational schools: in 1900 only 12.5% of municipal education expenditure went to high schools and 87.5% to public schools, but now only 69% goes to primary, 20% to high and 11% to vocational schools. Since the average cost per

pupil is higher in secondary schools, this change has been important in raising total costs. At the same time, the general educational standards in personnel and equipment were raised and the average cost per pupil in primary schools rose from \$17.8 in 1900 to \$74.1 in 1930, since when it has been reduced to \$60.6, the lowest since 1921. So far as provincial grants to schools are concerned, the existing method was introduced largely in 1931. The grants are based on five factors - a measure of the wealth of districts, the ratio of teachers' salaries to this assessment measure, the equipment, especially in rural districts, the basis of maintenance and capital expenditure on equalized assessments of schoolrooms, and teachers' certificates in rural and separate schools. These form the main method of grants although special grants and aids may be given to especially needy areas, or for special projects (kindergartens, manual training, etc.). These school grants (including grants to technical schools which rose rapidly from 1928 to 1930) have tended to become an increasing portion of the total provincial expenditure on education, and now average around 50% of that total. The remainder of the provincial expenditure goes mainly to universities (21% of the total education costs to the province), and the smaller part to agricultural and veterinary colleges, school inspectors, superannuation, etc. The university grants began in 1906 and have been enlarged with the extension of universities and the College of Education in Toronto. The total provincial education expenditures were lowered after 1931, mainly by the reduction of grants to primary schools, but the expenditure began to rise again in 1936.

Over 75% of Ontario's expenditures go on the three services described above - net debt, welfare and education. Of the remainder of the expenditure, the largest single item is the highways maintenance. This service reached its peak in 1930, 42% of the highway expenditure going to the maintenance of main roads and 40% in grants to municipalities, these grants being

mainly for construction. The remainder of the highway expenditure went to secondary roads and administration. The highway expenditure was severe in the depression, particularly the expenditure on main roads, although this reduction did not necessarily involve much reduction in road servicing since capital expenditures on roads, directly and through relief works were increasing at the time. Since 1933 the expenditure on maintenance of main roads has recovered, but in 1936 they still received a smaller percentage of the highway expenditure than in 1930.

Of the remaining services, justice, legislation and government have expanded in response to the enlargement of governmental functions but their growth has been checked since 1930. Public domain and agricultural services have also contracted since the advent of the depression, although in the public domain the provincial attention to forest services has expanded, but this expansion has been more than offset by the declines in attention to other sections of the domain.

On the revenue side, the main trend in the post-war period up to 1930 was the growing importance of taxes and of liquor profits in the revenue system. Tax revenues became a significant proportion of total revenues during the war period, and this significance has tended to increase. In 1913 taxes yielded 22% of the revenues, in 1921, 45%, and in 1930, 50%. The tax history of the later period, especially after 1934, further reinforced this trend, and by 1936 taxes yielded 60% of the revenues (as against 51% in the provinces as a whole). During this period, Ontario's share of the total revenues raised by all provinces has tended to increase. In 1921 Ontario's revenues were 24% of all provincial revenues: in 1928 29%, in 1930 33%, in 1933 36%, and in 1936 39%. This trend towards higher tax revenues advanced with the growing economic maturity of the province during and after the War. The shifts in the revenue system between 1921 and 1930 are shown in the following table:

	1921	1930 ($000)	Increase	Decrease
Dominion Subsidies	2,396	2,642	246	
Taxes	9,824	29,446	19,622	
Liquor Control	349	10,285	9,936	
Licences	4,313	7,682	3,369	
Refunds: Municipalities	100	2,577	2,477	
Domain	3,725	4,300	575	
Refunds: Other	91	537	446	
Other Revenue	105	135	30	
Sales	332	360	28	
Fines	672	434		238
Total	21,907	58,398	36,491	

About half of the rise in taxes resulted from the introduction of gasoline taxes (1925) which were yielding $10.8 million by 1930. In 1930 succession duties were unusually high, $6 million above the 1921 level. The corporation taxes had shown little increase up to 1930, but the adjustments of corporation tax rates that took place later in the depression indicated their potential yield.

The increase in liquor profits followed on the establishment of the trade as a government monopoly. The legislation establishing the Liquor Control Board was passed in 1927, and the sales rose rapidly in the boom years, but by 1933 liquor profits were only about half their 1929 level.

The increase in licences followed mainly on the expansion of the motor industry. Domain revenues in 1930 were still above their 1921 level, but forest revenues had fallen considerably below their 1929 level. The diversity of the revenue system, however, prevented a decline in any single item of revenue from having a great effect on revenue as a whole. As a result of industrial diversity and level of income, the revenues in Ontario fell by only 6% between 1930 and 1934, a large increase in motor licence revenues, and increases in corporation and gasoline taxes offsetting to a large extent the declines that were occurring in liquor profits, domain revenues and interest (other than hydro).

Although revenues were well maintained, they were not sufficient, in the depression, to cover expenditures and relief. There resulted large deficits on current account up to 1936, and since capital expenditures (except in 1933) had kept high, the over-all deficit was large until 1936, when an over-all surplus emerged. The position was as follows (omitting year 1935, which because of the change in fiscal year, was a seventeen month period, and apt therefore to confuse the significant changes that occurred between 1934 and 1936):-

(Millions of $)

	1931	1932	1933	1934	1936
Revenue	57.1	55.0	54.8	54.6	86.9
Expenditure	65.3	69.3	67.8	80.4	76.9
Deficit (-) or Surplus (+)	-8.2	-14.3	-13.0	-25.8	+10.0
Capital expenditure	28.9	27.4	13.7	35.5	7.5
Over-all deficit (-) or surplus(+)	-37.1	-41.7	-26.7	-61.3	+ 2.5

The current deficit which had reached a peak of over $25 million in 1934 was eliminated by 1936 as a result of the 59% increase in revenue,and the reduction in expenditure. The capital expenditures which had kept high (except in the low depression year 1933) were cut in the advanced recovery year 1936, and there was a reduction of $11.6 million in outstanding debt in that year.

The capital expenditures kept high until 1934 because relief work reached its peak in that year: the advances to the Agricultural Development were also high until 1934. As a result, capital expenditures on buildings (which had been $4.2 million in 1932) gradually fell to $1,191,000 in 1934 and $468,000 in 1936. Highway work, which had reached $17.6 million in 1931,

fell to $4.3 million in 1933, rose to $12.2 million in 1934 and fell again to $5.8 million in 1936. The reduction in highway expenditure was largely compensated by the increased relief work on highways, and the expenditure on this item rose from $1.4 million in 1931 to $19.2 million in 1934, and fell to $2.5 million by 1936.

As shown in the above table, both revenues and expenditures were by 1936 considerably above the 1931 level. With respect to expenditures, only the net debt charges and the welfare services had increased during the period, and even within the group of "welfare" certain services had been cut (e.g. public health, provincial institutions, child welfare, labour department). The welfare increase was due primarily to the relief payments which cost the province $13.3 million in 1936, but during the period there had been also some increase in mothers' allowances. The debt charges rose with the increase in the outstanding debt from $553 million in 1930 to $784 million in 1936. This increase was due in large part to depression financing. Of the debt increase of $231 million in these years, $50 million had gone to relief work on roads, and $73 million to current deficits including $14 million of direct relief. Of the remainder of the debt increase, 65% was attributable to public works, mainly roads, and the remainder to the hydro, the railway and the agricultural loan board. As a result of this increase, net debt charges absorbed 25% of the 1936 expenditure, and welfare (including relief) 37%. The expenditures were as follows:

	1930	1936	Increase	Decrease
		($ 000)		
Welfare	12,851	28,230	15,379	
Net Debt	9,659	19,397	9,738	
Education	12,895	10,564		2,331
Domain	4,595	2,787		1,808
Highways	6,836	5,397		1,439
Other	2,756	2,422		334
Legislation	1,024	339		685
Agriculture	1,357	872		485
Justice	3,128	2,715		413
Government	4,328	4,191		137
Total expenditure	59,429	76,914	17,485	

This table indicates the extent to which services, other than debt and welfare (including relief) have been reduced below the 1930 level.

Summary -

(1) By 1937, 41% of the total provincial gross funded debt was attributable to Ontario, Ontario's funded debt including guarantees being $748.1 million at that time. Of the growth of total outstanding provincial debt since 1929, Ontario's share was also about 41%, Ontario's outstanding debt having risen by $297 million from 1929 to 1936. In 1936, Ontario succeeded in reducing its outstanding debt by $11.6 million but by 1936, as a result of the growth of non-interest producing debt, Ontario's debt charges, less interest received, as a proportion of total expenditure, were higher than in the provinces as a whole, Ontario spending 25.2% of its expenditure on net debt, and the provinces as a whole 21.2%.

(2) By 1936, Ontario with 41% of the total provincial debt, raised 38% of the total provincial revenues. It got more revenue from taxation than other provinces, 60% as against 51%. It received a smaller proportion from subsidies, domain, liquor and licences.

(3) By 1936 Ontario was able to meet relief charges from revenue, and to lower its debt. But in 1936 all services (except debt charges and welfare) had been cut by $7.6 million under their 1930 level. In 1936 capital expenditures were exceptionally low. Tax revenues had increased by 77% between 1934 and 1936, and certain other revenues, licences, liquor profits and domain revenues were stimulated by the economic recovery, but in 1936 only licences had exceeded the boom peak. The significant revenue increase came from taxes, from the new rates, and from the economic recovery that increased income. Tax revenues rose by $23 million between 1934 and 1936, succession duties producing 42% of the increase, corporation

taxes 15%, gasoline tax 12%, income tax 22%, amusement tax 6%, and the security tax 3%. Succession duties, which had yielded half of the tax revenues in 1921, yielded one-third in 1925 and one quarter in 1933. The extensive changes in the Succession Duty Act in 1934, with the further amendments in 1935 and 1937, have tended to restore succession duties to their 1925 place in the tax picture, that is, to the production of one-third of the total tax revenues. Up to 1930 corporation taxes had been comparatively stable, but the capital stock and the new taxes on net income by 1936 restored these taxes also to their 1925 position, to the production of about one-fifth of the tax revenues. Given no further economic recession, the corporation taxes may prove to be on a more stable revenue-producing basis than the 1936 succession duties. The other significant tax change was the introduction of the income tax in 1936. If the province pursues the policy of raising tax rates, and therefore revenues, in the recovery years, and if it holds down its capital works and reduces its debts in these years, it will be pursuing a fiscal policy that has had no counterpart in Canada's public finance. But final comment on the precise nature of Ontario's fiscal policy would have to be reserved until the nature of the policy pursued in any future depression was revealed.

(4) The revenue position of the province reflects the economic maturity of Ontario. Its economic position as the "Workshop" of Canada, as an important exporter, as a mining area and as a provider of services (tourist and other), indicates a certain balance that is important from the point of view of revenues. The number and kind of firms and their corporate organization, and the number of households and the sort of living standards established by the economic productivity combine to produce a provincial economy that has considerable taxable capacity. The number of firms and their organization affects the level of corporation taxes, while the productivity of these firms, as reflected in the income of households, affects the levels of succession duties, income tax, amusement

taxes, automobile licence fees and gasoline taxes, etc. These sources provide about three-quarters of Ontario's total revenue.

As a revenue-producer Ontario's economy is important also to the Dominion government, which derives a very significant proportion of its total revenues from this mature region. This circumstance is of prime importance to the province of Ontario as well as to the firms and households located there. It is important to the province because the Dominion revenue methods affect the province's revenue possibilities. To the households and firms in the region the resulting fiscal situation is important since two major tax authorities compete for revenues in the region, and there can be no presumption that their combined revenue methods will yield a tax system that is just, or least harmful to enterprise. This situation confronting the households and firms of Ontario (and to a lesser extent of Quebec) is worthy of attention, especially since the expenditures of both the Dominion and provincial governments are likely to continue moving upwards, and since any depression tends to add to governmental responsibilities, and presumably governmental revenue efforts. A fall in national income or even a fall in the income of any region of Canada adds to Dominion responsibilities, tends to expand the Dominion's revenue efforts, and therefore tends to limit the Province of Ontario's revenue possibilities. And as the Dominion tax system becomes increasingly direct and increasingly graduated, the concern of the government and taxpayers of Ontario is increased, since these changes tend to increase the burden on incomes of Ontario households and firms. In short, Ontario is greatly concerned in the level of national

income, and in the effects of that level on Dominion fiscal action. Firms and households of Ontario are perhaps more deeply concerned than the provincial government, because the division of powers between governments tends to hide the fact that the provincial and Dominion governments compete for the available revenues. It appears on the surface as if their fiscal requirements are determined by economic conditions. Depression adds to their responsibilities, raises debts and requires new tax efforts: the boom works in the opposite direction; and so it appears that the fiscal policy of independent governments, acting separately, is largely determined for them, yet it is unquestionable that fiscal policy as a whole affects the level of national income, and the trend towards boom or depression. Fiscal policy as a whole, especially at the present levels of expenditure and taxation, affects the behaviour of households and firms, and this behaviour in turn affects the trend of economic progress. As a force on the economy, fiscal policy is probably of more importance than banking or exchange policy. Since a wise co-ordination of fiscal policy can aid the forces that make for reduced expenditure needs, and increased revenue buoyancies for all governments, and since the future of Ontario is so closely connected with the future of the Canadian national income, this question of the co-ordination of fiscal policy affects the future of the firms in Ontario to an exceptional degree.

(5) But the extent to which the Dominion or Ontario government can pursue any fiscal policy designed to counteract trade fluctuations, or to encourage home industry, is determined partly by the actions of the other government. If Ontario should wish to hold up tax rates in boom periods and reduce capital expenditures and debts, as she did in 1936, and if then the Dominion also raised its tax rates, this would involve some limitation on the expansion of the province's revenues, since the Dominion gets so large a share of its revenues from this province. Oppositely if the Dominion reduced its taxes in the

boom , then it would leave more spending power and more taxable capacity to the province. In depression, if the province wished to reduce taxes to try to encourage local industry, the beneficial effect of such action would be lost if the Dominion government raised its taxes. In such a case the province would be merely transferring taxable capacity to the Dominion government.

The fact that so much of the national income is derived from this province, and that so much of the federal revenue has its source there, is sufficient to decide that no Canadian fiscal policy is likely to be successful in smoothing out trade fluctuations - unless there is careful integration of the expenditures and the taxes of the Dominion and the Ontario governments.

Financial Position of Manitoba

Up to the end of the 19th century, Manitoba's financial history reflected the growth of the province. For detailed study, this early formative stage could be further subdivided, but for general purposes it seems sufficient to indicate the conditions that characterized the period up to the end of what was termed abroad the Great Depression (1896).

During this period the features of Manitoba public finance were absence of any significant debt charge, great dependence on the Dominion subsidy for revenues, inability to keep expenditures in line with revenues, and a great preponderance of costs of government and of public works in the distribution of total expenditures. All these indicate the youthful stage. The preponderance of government and equipment costs could be compared to the education charges of the individual in the same stage of growth, and the dependence on the subsidy is comparable to the youthful individual's dependence on the family. But Manitoba's formative history was affected by the fact that she did not grow into the responsibility of government, but had that responsibility imposed on her in her earliest pioneer stage. She had still to acquire institutions, roads and the equipment of settlement, and since her revenues were supplied largely from the Dominion (e.g. as high as 88% in 1875), and since she lacked territorial revenues, the process of acquiring governmental equipment was largely a process of readjusting financial relations with the Dominion. Thus the frequent changes that occurred in the Dominion subsidy to Manitoba, almost from the creation of the province up to 1913, were to be expected. That the experience had some value to the Dominion may be judged from the subsidy arrangements made with the new prairie provinces created in 1905. That the responsibility of government, and the pains of growth, were creating a positive opinion within Manitoba was evident from the provincial government's attitude

toward transport.[1] It has been said that the natural resources question, opened in the 80's, the complaints about the federal tariff, and the grievance against the Canadian Pacific Railway monopoly, were weapons found to fight the subsidy case with the Dominion. But the fact that the weapons did exist, and were used, indicated that ideas of development, and of the forces that hindered development, were being shaped in the Province, and these turned largely on the transport issue. Dominion plans and regulations concerning land holdings were extensive, and the plans were altered periodically to suit the construction needs of the Canadian Pacific Railway at this time; but this uncertainty was not favourable to settlement in the Province. Where settlement was well advanced and the fertility of the country was reflected in increased wheat production, the lack of effective means for marketing the grain proved a deterrent. These needs became more apparent after the Canadian Pacific line reached Winnipeg in 1883. The railway monopoly and the needs of the economy for branch lines and cheaper rail rates provided a target and ammunition for the government that was growing into fiscal responsibility. Winnipeg was by then thinking of its possible future as the commercial entrepot of the West, and for its promotion as a distribution centre transport was a vital issue. Accordingly, Manitoba's first bond issue ($787,000) in 1885, was for a construction subsidy to the Manitoba and Northwestern Railway. Others followed for the Brandon and Southwestern, for branch lines, and for a railway to Hudson Bay. The municipalities were given permission to give railway subsidies, exemption from provincial and municipal taxation was offered as an inducement to railway construction and, most important of all, the methods of guaranteeing railway bonds was adopted. In 1888 the Province guaranteed bonds of the Northern Pacific

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(1) Maxwell, J. A. Federal Subsidies to the Provincial Governments, p. 81.

and Manitoba Railway, and in 1889 and 1892 bond guarantees were offered to the Hudson Bay and to the Lake Manitoba Railways. The presence of MacKenzie and Mann aided the province in pushing this railway policy still further, and in 1901 guarantees were given to the new Canadian Northern Railway to complete a line from Winnipeg to Port Arthur.

The adoption of the railway policy is some indication of the growth of responsibility towards the end of the century. The change in the ordinary budget also reflected the end of the formative stage in the province's financial history. On current account, new expenditures on education, public domain, and welfare, began to compete with the costs of government and public works for the available revenues. On the revenue side, corporation taxes and later succession duties and railway taxes were imposed, the revenue from fees was increased, and so also were the returns received from interest. By 1900 just less than 50% of the revenues came from the Dominion subsidy, and the remainder was secured by the province's own revenue efforts. Revenues were not buoyant in the last decade of the 19th Century, and the general depression in agriculture was an important contributor to the province's efforts to broaden its revenue base. During the depression the debt charges and public welfare tended to absorb an increasing share of the available revenue, but total expenditures were kept in check, and they were smaller per head in 1901 than in 1891.

The rise in world prices after 1896 and low freight charges increased the profitability of grain production. Railway expansion, and readily available supplies of capital provided the means for fuller specialization in wheat. The rise in prices continued through the pre-war and war years. The expansion of wheat acreage and elevator capacity turned sharply upwards in 1901, and in 1902 Manitoba's revenues reflected the sudden change in wheat income after the 1900 drought. Half the prairie population was then in Manitoba, and she had already 1500 miles of railway, so that the returns that were apparent from her pioneering soon encouraged

the westward expansion of settlement, railways, and new wheat acreage. After this, Manitoba's rate of growth was slower than that of the other two provinces, but the boom period up to 1912 consolidated Winnipeg's position as the commercial and manufacturing centre of the new prairie region, and the fact that Manitoba had inaugurated her railway policy early, and had some governmental experience, permitted her to adjust her economy to expansion with less difficulty. Expansion of revenue and consistent surpluses on ordinary account from 1901 to 1912, were evidence of stability.

Significant borrowing on direct bonds did not begin in Manitoba until after the creation of the two other prairie provinces, but once started it reached comparatively high peaks in 1907, 1910, 1915 and 1920. The 1907 peak was due almost entirely to the initiation of government telephones: the 1910 peak was associated with grain elevator purchases and construction of judiciary building: the 1915 one with the building of the agricultural college, insane hospitals, and the new Parliamentary Buildings: and the 1920 one with new government enterprises connected with agriculture, the power commission, and certain patriotic expenditures, including relief of taxation to soldiers. As a result, between 1907 and 1921 the gross debt of Manitoba grew more than in Saskatchewan, and about as much as in Alberta and British Columbia.

The telephone policy began with a bond issue of $1 million in 1907, followed by another of $3.4 million to buy out the Bell system. There were then about 15,000 subscribers in the province. Administration was entrusted to a Commission, and for the next four years capitalization increased, although the Commission found it difficult to expand quickly enough to keep up with the demand. The state of the telephone accounts during this period did little to reveal the financial condition of the enterprise, and the telephone commission felt that some rate adjustment was necessary in 1911 to add to revenues. The

suggested change was unpopular and investigation by a royal commission suggested the need for removing the telephone system from political interference. No important changes were made, although some flat increases in rates were sanctioned by the new rate controlling body, the Public Utilities Commission, but these changes were not sufficient to meet the revenue needs of the system.(1) During the war period, the system was handled with more attention to economy, and in 1918 comprehensive depreciation tables were constructed. Wages and other costs climbed high at the end of the War but no changes were made in rates and from 1919 to 1921 considerable financial losses were incurred. In 1921 rate increases were allowed, the greatest being on the rural lines.

By 1920, the system had 69,000 subscribers as against 15,000 in 1907. This may indicate that government ownership did spread the system quickly, but considering that in this period the economy rapidly expanded and that there was a fairly well established private telephone system in Manitoba in 1907, it is impossible to know whether government ownership did in fact speed up the system more than private enterprise could or would have done. The question is whether private enterprise could have been efficient and could have provided service at lower rates than the government did, when the government took over ownership. Manitoba had the foundations of a system better laid than Alberta and a more favourable ratio of urban to rural service - extensive rural systems being costly. These two conditions rendered somewhat easier the economic expansion of Manitoba's service. The tendency to over-expand the rural part of the systems was sooner checked in Manitoba, and the existence of a metropolitan area and metropolitan opinion may not be

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(1) By 1913, the province had invested over $11 million in telephones.

unconnected with Manitoba's earlier attentions to more economic management and more care over depreciation. Nevertheless, the influence of telephone policy on the growth of Manitoba's debt was important from 1907 to 1913, and at the latter date the government investment in telephones accounted for about half of the gross debt.

The other factors contributing to the pre-war debt growth seem to have been directly associated with the frontier expansion. The birth of the Grain Growers' Grain Company in 1906 was associated with the apparent insignificance of the individual producer in the new economy, and was directed at co-operative efforts that would strengthen the farmer in his marketing. The Association urged among other things, the construction of a Hudson Bay railway, and government ownership of terminal and internal elevators, and in 1910 the latter question became a political issue in Manitoba. Without making investigations, such as were undertaken by Saskatchewan, the Manitoba government adopted the proposal and started off with a purchase of 75 elevators. When the scheme came into operation after the election, difficulties arose. The growers desired a reduction in the elevator commission from 1 cent to one-half cent, and at the same time demands for new government elevators were strong. These were more expensive than telephones, from the government's point of view, and they were not yielding adequate revenue. By 1912, it was decided that the policy was a mistake and 172 elevators were leased to the Grain Growers' Company at 6% on the government's investment. The experiment, though not pushed very far, convinced opinion that co-operation rather than government ownership was the right means of overcoming the isolation of the producer from markets. The capital advanced to elevators was given as $1 million in the 1913 balance sheet, but since the revenues and expenditures of the elevators have been incorporated in the main provincial accounts, it is not easy to discover their later operating deficits. The "capital" loss has been shown

as $705,000, in the balance sheets from 1927 onwards.

The other works that added to the 1910 peak in borrowing were judicial buildings. Thereafter expenditure on the drainage districts and new public buildings became the most significant, especially the latter. These were projected when the pre-war economic expansion was nearing its maximum, and when Winnipeg was rapidly becoming the metropolitan area for the new prairie economy. Some of the public works were large, especially the Parliamentary buildings, but the new mental institutions, law courts and agricultural college buildings were also conceived on the grand expectations of the boom period.

Thus while the 1913 gross debt figures showed a total for Manitoba that was below Alberta's, and about 15% higher than Saskatchewan's, the conditions that were increasing the rate of Manitoba's debt as compared with Saskatchewan's were already in existence. And the recession of trade before the outbreak of War, the slowing of immigration, and the approach of the completion of the railway boom were not likely to be factors that would check the expansion of governmental activities. Indeed the apparent thwarting of pre-war expectations was more likely to increase the demand for government activity. The exigencies of the War itself furthered this movement, especially in the relations of government with agriculture. The pre-war administration had directed its attentions to the provision of general equipment (buildings, encouragement of railways, etc.). Its attempts to assist agriculture had proved less satisfactory. In the early war period, when the equipment boom had fulfilled its purposes, and agriculture was encountering difficulties, the shift of government attention to agriculture's needs was to be expected.

The most important government assistance to agriculture, from the point of view of debt growth, was the establishment of the Farm Loans Association in 1917, aimed at the provision of loans at reduced interest rates. It obtained capital by issuing bonds

carrying the guarantee of the province and the pledge of farm mortgage as security. Up to 1921, the interest to the mortgagor was 6% per annum, combined with a subscription to the capital stock of the Association, to the extent of 5% of the loan. In 1921 the latter requirement was withdrawn, and interest charges raised to 7%, until in 1925 the Association began financing through the treasury of the province and managed to lower rates on new borrowing to 6½%.

This governmental assistance in the form of farm loans was superimposed on a government building programme that was to continue large until 1920. In 1918 a good roads policy was added, then in 1919 a housing policy, and in 1920 a power policy. As a result, the investments of the Province of Manitoba in equipment (housing, buildings, roads, telephone expansion, power commission), as well as the agricultural aids, added together significantly in the 1918-20 period, the latter year representing a peak in the province's issuing of bonds.

The effect of all these government policies was to make the rate of debt increase between 1913 and 1921 particularly high in Manitoba as compared with other provinces, the steep upthrust occurring just at the end of the War when all the policies (public works, telephones, power, roads, housing, agriculture) required funds, and the general post-war boom was pushing up prices. The Manitoba government's investment in this period probably accelerated the local boom, When the general boom broke in 1921, the government's building policy probably helped to account for the maintenance of the local construction industry in 1921, but with the decline in government building in the following year, the construction industry contracted and failed to recover its 1921 level until 1926. The power industry expanded slowly throughout the period.

The effects of the various policies, and their quantitative significance are evident from the balance sheet.

Between 1913 and 1921, the assets expanded as follows:-

$ million

		1913		1921	Increase	Decrease
Active Assets		1.7		10.4	8.7	
Utilities (a)		36.1		20.2		15.9
Public Works		9.2		27.5	18.3	
Advances		3.4		17.5	14.1	
Current Deficit		-		.8	.8	
		50.4		76.4	26.0	
Less Sinking Fund						
Reserve	.4		1.2			
Capital Surplus	4.4		2.7			
Deferred Revenue	-	4.8	.3	4.2	- .6	
Outstanding Debt		45.6		72.2	26.6	

(a) Includes $24 million Canadian Northern Railway guarantees later assumed by the Canadian National Railways.

The $27 million increase in debt was due largely to the public works and the advances, the utilities and the active assets together having added less than the public works. In the public works expenditures, highways were comparatively unimportant, the main outlay having been on public buildings. The most significant single expenditure under this head was the new parliamentary building, although as already shown, expenditures on the agricultural college and the mental hospitals at Selkirk and Brandon, when combined, formed a part of the total increase in public works.

As the above table shows, the second important contributor to the debt increase was the $14 million increase in advances. In this disbursement, the Farm Loan Association had received the largest share($5.6 million by 1921), the housing scheme was next at $3.4 million, then the rural credit societies ($2.6 million), soldiers tax relief and patriotic purposes ($1.3 million), and the remainder on miscellaneous advances, including the investigation of public buildings, seed grain and fodder loans, drainage, etc.

An additional investment of $6 million went into telephones, and $1.8 million into the recently established power commission in the 1913-21 period. This equalled nearly half the expenditure on public works. The decrease in the total investment in

utilities was due to the assumption of $24 million Canadian Northern Railways bonds by the newly formed Canadian National Railways.

As a result of this large debt increase the net debt charges, which had amounted to $604,000 in 1913, had increased to over $1,217,000 in 1921, and at the latter date net debt absorbed 15% of the total expenditures. The other important increases in current expenditures were in public welfare and in education. Welfare rose from $406,000 to $1.9 million, partly as a result of the Mothers' Allowance Act in 1915, and partly as a result of the levels of cost of maintenance and operation in the new hospitals. Other welfare activities (e.g. public health, and labour) took insignificant sums. In education, the increase was comparable to that on welfare, the expenditure having risen from $737,000 to $2 million. In 1921 it absorbed 25% of the total expenditure, and most of the increase went to school grants, with colleges and universities taking the remainder. These three items, net debt charges, education and welfare, absorbed 62% of the expenditure. Government, legislation and justice absorbed 25% so that amounts spent on other services - highways, agriculture, domain - were very small. The expenditure system was already dominated by expenditures that were difficult to contract, if depression made that policy appear desirable.

During this period of rising expenditures, the revenue basis had been gradually broadened. In 1913 revenues were largely dependent on the Dominion subsidy, licences, and the public domain. In that year, however, corporation taxes were increased, and in 1915 automobile licences were doubled. Thereupon followed further attempts to widen the tax base by the addition of amusement taxes in 1915. In 1916 the Municipal Commissioner was authorized to make a levy for mothers' allowances. In the following years further levies were made, notably the supplementary Revenue levy in 1918, which was increased in 1919 and 1920, and which was levied on all municipalities and on property in school districts. In 1918 a tax was imposed on unoccupied land. As a result of this broadening of the tax basis, in 1921 the Dominion subsidy formed only 20% of the total revenues, and was less important than the

taxes on real property (i.e. supplementary revenue tax, and unoccupied land tax) as a producer of revenue. The corporation taxes were now yielding a larger part of the revenue, especially the railway and insurance companies. The motor vehicle licences were becoming productive, and the government capital expenditures were yielding new levels of interest. The following table shows the increases in revenues between 1913 and 1921:-

REVENUE
$000

	1913	1921	Increase	Decrease
Taxes	645	3,751	3,106	
Licences	596	1,176	580	
Subsidy	1,451	1,471	20	
Domain	427	256		171
Liquor	162	80		82
Others	813	644		169
Total Revenue	4,094	7,378	3,284	

The revenue changes revealed the extent to which the tax basis had been broadened, as a result of the new scale of government activities during the War and post-war years. In 1921, the debt charges, less interest received, still formed only 15% of Manitoba's expenditures, while the figure for all provinces was 16%.

In the depression of 1921 however, tax returns fell, especially the corporation taxes, amusement taxes and succession duties. This contraction continued through 1922. At the same time the government encountered deficits on some of its enterprises, as well as a certain fixity in ordinary expenditures that rendered their reduction difficult. The necessity for having a proper sinking fund provision for debt redemption became obvious.

During the depression, certain readjustments were made in the subsidiary enterprises of the government, and in the tax system. The telephone system was placed on a fairly sound footing, the power commission was reorganized, and a certain

amount of liquidation occurred in the Farm Loans Association, the Rural Credit Schemes, and the government elevators.

The telephone system entered the post-war period with considerable need for rate increases, which rates, despite the post-war rise in costs, had remained unchanged from 1912. The rates were raised by an average of 28% in 1921, the rural increase being above this. The ensuing depression in agriculture contracted the rural demand for telephones by 25%, and at the same time the provincial exchanges, i.e. the urban communities outside Winnipeg, also revealed a decline in demand. Fortunately, however, the Winnipeg exchange kept up, and the telephone system devoted most of its new capital expenditure to the modernizing of this urban plant from 1922 to 1928. (During this period, the automatic service was installed, and by 1928 two new exchanges were required in Winnipeg. The City's demand for telephones reflected its strong economic position in the good "wheat" years from 1925 to 1928). At the same time, any tendency to over-expansion of the rural system was checked, and as a result deficits disappeared. In the boom years from 1925 on to 1929, the deficits gave way to surpluses even after a proper allowance for maintenance and replacement of plant. The government telephone investment had been $17 million in 1921, but by 1929 the figure had reached almost $22 million.

The Power Commission which had been conceived in the post-war boom days -- a period that was often regarded as the natural continuance of the boom that had been shortened by the outbreak of War -- had been projected on optimistic expectations of future development, and therefore of demand for power. The post-war depression confounded these expectations, and the Sullivan Commission, appointed in 1923 to study the difficulties that were being encountered by the provincial power company, found that the enterprise had been commenced before the population, or the demand for energy, was sufficient to justify the expenditure -- a circumstance that had been true of many of the

prairie government enterprises in the early 20th Century, but in many cases the rate of economic expansion had "taken up the slack" and had reduced excess capacity. The post-war depression, however, had thwarted the expectations as to power demand in Manitoba, and in 1923, even if the contracts had been doubled, there would still have been a deficit. The fact that the system had been built in a period of high prices added to the cost difficulty. Following the Sullivan recommendations, the government in 1925 reduced the capitalization of the Power Commission, the province assuming the difference between the old and new appraisals in its own debt, transferring part of the advances to a suspense account, on which part no interest was charged to the Commission, and reducing the rate of interest charged to the Commission from 6% to 5%. The 1925 Act also established a sinking fund and reserves for the Commission. In 1921 the capital advances to the Power Commission had been $1.8 million. In 1925 they were $2 million, and $0.6 million had been transferred to capital losses.

The Farm Loans Association had made considerable loans in the prosperous agricultural boom from 1917-20, and these had been used either to pay off prior mortgages held by private mortgage companies, or for agricultural expansion. In 1921 further loans were sought, and in view of the agricultural depression, it is probable that these were intended more to maintain the position of the borrowers than to expand their undertakings. By 1923, over $8 million had been advanced, but thereafter loans were smaller up to 1930, when new loans were stopped. The advent of the 1921 depression had revealed certain inherent weaknesses in the schemes. It revealed the fact that, with the wide fluctuations in agricultural income, mortgagors were liable to fall sharply into arrears when depression hit them, and the more severe the depression the greater the likelihood of arrears. In such a case the association had either to foreclose, or capitalize the arrears and give new

mortgages on the basis of the principal and the arrears. In principle, therefore, the Association showed some tendency towards (a) relieving private mortgage companies of risk, especially bad "risks", who consolidated their debts in a loan from the Association (b) feeling the necessity of maintaining its borrowers in event of stress. To some extent, the latter condition arose from the technique of repayment, which required borrowers to repay the principal and interest of their loans in 30 equal instalments. This period was long, and was more suited to a borrower who was assured of a steady income than to agriculturalists who faced the vagaries of crop and market changes. In these conditions also, it appears as if the interest rate charged to borrowers was insufficient to leave the Association a wide enough margin for risk, while at the same time, it was sufficiently attractive to encourage a fair demand for loans. By 1925, the advances to the Farm Loans Association reached $9.5 million, and in 1929 when the federal farm loan scheme began operations in Manitoba - after which the provincial Association ceased to issue new loans - the province had advanced $10.2 million to its own Association.

During the post-war depression therefore considerable headway was made in writing-off the losses involved by the War and post-war investments. But the outstanding debt continued to grow, rising from $72 million in 1921 to $88 million in 1925. As mentioned above, the Farm Loans Association advances had increased from $5.6 million to $9.5 million in this period: that represented the largest single item. The investment in telephones, buildings, and highways added approximately $2 million to each of these services. Although this involved an increase in net debt charges from $1.2 million to $2.3 million, current expenditures were kept in check and their level in 1925 was only a little above that of 1921. At the same time, the province made marked changes in its revenue system in this readjustment period, and revenues, which had failed to cover

expenditures in 1921, rose from $7.4 million to $9.6 million by 1925 and since expenditures had varied little, the $888,000 current deficit of 1921 had become a $509,000 surplus by 1925. The most significant changes in the revenue system were the imposition of the gasoline tax and the income tax in 1923. In 1921 and 1923 the automobile licences were increased, and in 1924 additions were made to the corporation taxes and to succession duties. A "betting" (or pari-mutuel) tax was imposed, and a grain futures tax, which was later declared ultra vires. With these changes, and with the improvement in trade after 1924, revenues began to rise steadily. The revenues in 1925 were as follows:

	MANITOBA		ALL PROVINCES
	Revenues $000	% of Total	% of Total
Subsidy	1,502	16	10
Taxes	4,827	50	39
Licences	1,246	13	18
Liquor	1,315	14	13
Others	706	7	20
Total	9,596	100	100

Manitoba was receiving a larger proportion of its revenues from taxes and interest than the provinces as a whole.

In 1926 Manitoba's revenues continued to rise more than the expenditures, and a larger surplus emerged. About this time, there was evidence of a transition from public "economy" to public spending, not on the scale of the post-war boom years, but nevertheless, in contrast to the policy in the post-war depression years. The transition showed itself in three ways, in the rise of current expenditures, in rise of capital expenditures, and in the reduction of tax rates. The boom was not sufficiently great to hold up revenues in face of the tax reductions, and deficits resulted, as

follows:-

	$000		
	1926	1927	1928
Revenues	10,290	9,401	10,255
Expenditures	8,987	9,420	10,187
Surplus (+) or Deficit (-)	+ 1,303	- 19	+ 68
Capital Expenditures	1,257	1,123	3,033
Over-all Surplus (+) or Deficit (-)	+ 46	-1,142	- 2,965

The fall in revenues in 1927 resulted from the fall in tax returns, which in turn resulted from the 20% reduction in income tax, and the reduction from 2 mills to 1¼ in the supplementary revenue (land) tax. In addition it had been decided that future surpluses should be used to reduce the land tax, and in small part, the income tax. As a result, tax revenues declined from $5.4 million in 1926 to $4.4 million in 1927, and the current surplus of 1926 had been transformed into a deficit. The province then cancelled the 1922 rebate to the municipalities of 50% of the liquor profits. In consequence liquor profits rose from $1.3 million in 1927 to $2.0 million in 1928, and revenues as a whole rose by about the same amount, and a small current surplus appeared in the boom year of 1928 (i.e. fiscal year ending April 1929). The decline in the importance of the land taxes was then becoming marked. At the end of the War, these taxes (the supplementary revenue and the unoccupied land) had formed about 20% of total revenues: by 1928 they formed about 3%. There had been strong rural opposition to these taxes, and in 1929 the province abolished the supplementary revenue tax, and the revenue system was depending more and more on non-land revenues. Later other minor land taxes were abolished -- the Health Levy, Child Welfare and Soldiers' Taxation Relief Levy. These changes benefited real estate, but even more so, they reduced the specific provincial taxes paid by the farmer. The province had only about one-third

of its population in agriculture (as compared with two-thirds in Saskatchewan), and it was building a revenue system that was appropriate to an urbanized province. But the urbanization in Manitoba was due, not to a diversification of industry, but to the fact that Winnipeg was the entrepot of the prairies. As such its income depended primarily on the agricultural income of the prairies as a whole. And it was only in conditions of boom in the prairies as a whole, that Manitoba could afford to make tax concessions to its own agriculturalists, or to give them special services at low cost (e.g. telephones, power), if the province wished to pursue an orthodox financial policy. In the event of depression in the prairies as a whole, the urban income in Manitoba was liable to severe contraction, and the commercial "overhead" of the prairie region, which was centred in Winnipeg, was liable to become a burden on the province, the costs of the overhead translating themselves into relief costs that would have to be borne by the province (including the municipality). In short, in depression, Winnipeg had to bear some of the impact of the decline in agricultural income in the prairies as a whole, and not merely the decline of Manitoba's agricultural income, and this in turn affected the expenditure requirements and revenue possibilities of the provincial government and the City. So long as the boom progressed, however, dependence on the extended hinterland was an advantage.

In the boom period also there was some rise in ordinary expenditures, particularly after 1928. The main increases were in welfare and highway expenditures, with smaller ones in debt charges and in education. In 1928, public welfare charges began to increase, mainly through introduction of old age pensions, and partly by expansion of public health services: in 1929 this upward movement continued, and welfare which had accounted for only 21% of total expenditure in 1925, amounted to 30% by 1929. The other expenditure that turned sharply upwards at this time was that on highways, the new

direction of expenditure being on main highways. The other expenditures were kept in check, the two above items accounting for over two-thirds of the expenditure growth in 1928 and 1929.

The increase in debt charges followed on the expansion of capital works that the boom seemed to encourage. These began with an expansion of highway services in 1927, and from 1928 to 1930 these averaged about $2.8 million annually. The continuance of the boom, however, led to other minor capital expenditures on public works, in 1928 to new investments in the telephones, and in 1929 and 1930 further investment in the Power Commission. For all its purposes, the province had required $10.1 million in 1926, but by 1929 its rise in current and capital expenditures had raised its total requirements to $16.2 million, and since its revenues had not risen to the same extent, the increase in outstanding debt was almost $5 million in each of the years 1928 and 1929. By 1929 the outstanding debt was $101.1 million, and Manitoba's annual debt charge (less interest receipts) began to take a higher proportion of its total expenditures than in the provinces as a whole (18% as against the general average of 17% in 1929).

While agricultural income fell in 1929, it was not until the following year that other parts of the Manitoba economy began to feel the effects of the decline in commerce and manufactures that were consequent on the prairie depression. The extent to which Winnipeg depended on the prosperity of the whole prairie region became clearer as the depression progressed and the only provincial industry that withstood the dislocation was the small mining industry.

Such conditions were likely to contract revenues almost irrespective of the kind of taxes utilized. At the same time, the land taxes were in process of withdrawal, as already indicated, and this contracted provincial revenues further, although it yielded some relief to farmers, leaving them with only a few taxes on spending (e.g. gasoline), and the few

remaining levies for old age pensions and sanatoria. In addition, some indirect subsidies were given to the people of the rural areas in both telephone and power services, the rates on these being below cost.

The government was faced, therefore, with contracting revenues, almost stable ordinary expenditures, and considerable capital commitments which the depression was rendering onerous. In such conditions adjustment of the financial position was rendered particularly difficult.

The income tax was widened to include corporations in 1930, imposing a 2% tax on income of corporations exceeding $1,000: in 1932 the rate was raised to 5% and the exemption removed. In 1931 the personal income tax was raised, and in 1932 the exemptions were lowered and surtax added. The gasoline tax was raised from 3 to 5 cents in 1930, and to 7 cents in 1932. In 1932 corporation taxes were increased. There was therefore, little delay in trying to catch more revenues, but most of the changes were more fitting to a highly industrialized economy: the rural areas were not directly affected by the increased rates, although of course they were greatly affected by reduced income. Despite the changes, revenues could not be maintained, and they fell considerably from 1929 to 1931, and remained on that level until 1933.

On its ordinary expenditures the province showed the same rush for cover quite early in the depression, cuts in some services being made in 1931, 1932 and 1933. By the latter year, current expenditures outside debt and relief charges, had been cut by 25% below their 1930 peak. The position was as follows:-

$ million	1930	1931	1932	1933
Total expenditures	12.5	14.4	15.4	14.6
Debt charges	1.8	3.2	5.0	4.4
Direct Relief and Provincial Share of Municipal Works	.5	2.1	2.0	2.5
All other Services	10.2	9.1	8.4	7.7

Among the other services, between 1930 and 1933, the

biggest cuts were in highways, ($733,000), welfare, excluding relief, ($874,000), all government ($568,000), and education ($503,000).

In 1929 public welfare, excluding relief, and education had together accounted for 48% of the total expenditures but by 1933 they had been cut by almost 21%, and absorbed only 30% of the total expenditure, there having been a paring down of expenditures on health, tuberculosis institutions, hospitals and pensions, and in education a large reduction in grants to schools. Highways, however, showed the biggest reduction, being cut by 44%. Apart from relief and debt the only service that showed even a slight increase between 1930 and 1933 was the public domain, some increase following the grant of natural resources in 1930.

The significant increase in debt charges followed on the financing of the early incidents of the depression. As we have seen, the province entered the depression carrying new commitments, and expanding capital works (roads, telephones, and power). In the early depression years, the position was as follows:-

Millions of Dollars

	1930	1931	1932
Highways	2.6	1.6	.1
Relief Works	.1	.8	.4
Other Public Works	.9	.5	.1
Co-operative Wheat Products	-	1.3	-
Other advances net	.4	.5	.9
Total Capital Expenditures	4.0	4.7	1.5

In 1930 the public works expenditure was directed mainly at highways, with small amounts on public buildings and on the university. In that year the deficit on ordinary account was $1.2 million, the capital expenditures (as shown above) $4.0 million so that the over-all deficit was $5.2 million. In addition to the covering of this deficit, funds were required also to continue the Hydro development that had been begun in the boom, and $1.8 million went also to the Power Commission. The telephone expansion required $0.8 million to complete it.

In that year however, the province received the settlement on the transfer of the natural resources from the Dominion, an amount of $4.6 million. Nevertheless in 1930 the outstanding debt rose by $6.5 million. In 1931 the financial position was affected by the deepening of the depression. The current deficit rose to $4.8 million, current expenditure being pushed up by direct relief (capitalized) by relief works of municipal authorities (provincial contribution), and by losses on exchange. These combined with the rise in the net debt charge raised the current expenditure from $12.5 million to $14.4 million in 1931, and since revenues fell by $1.6 million, the current deficit was high. Public works were down slightly from the previous year, but the over-all deficit rose to $9.4 million. In that year also the Provincial Savings Office was wound up, the Power Commission required another $1 million investment and advances were made to Manitoba Pool Elevators. Accordingly the funds required exceeded those of the previous year, and $8.4 million were added to debt. The province also had to implement its guarantees on the Farm Loans Association and the Co-operative Wheat Producers. In 1932, however, the province cut its capital expenditures and again in 1933, since when capital expenditures may be said to have ceased. By 1933 the cuts in ordinary expenditure were becoming effective, the losses on exchange were smaller, and new tax adjustments raised revenues so that the current deficit was cut from $4.9 million to $2.5 million between 1932 and 1933. The tax adjustments were far-reaching. They were raised in 1933 by the addition of a special income tax of 2% on all income of single persons receiving $480 or more (or married $960). This tax became straightway one of the most important revenue producers at the province's command, approximately equal to the corporation taxes, and just below the most important tax - the gasoline tax, the latter yielding about 14% of total revenue in 1936, and the corporation and wages taxes

each about 13%. Special income tax along with the former income tax totalled about 20% of revenues in 1936 whereas before the depression such direct taxes were comparatively unimportant, (and the special income tax non-existent). This is some indication of the increasing directness of the revenue system, and a measure of the attempt to tap whatever incomes were produced. The taxes on spending (e.g. liquor) fell greatly in the depression and have been slow to recover, indicating the shift in consumption under the reduced income-levels. The amusement taxes showed the same characteristic, although they never were highly significant. The net result was that while total revenues in 1933 were slightly greater than those of 1929, the liquor profits, land taxes, motor vehicle duties and succession duties had been the main producers in 1929, but the main 1933 sources were income taxes, corporation and gasoline taxes.

The history of the years following 1933 was the result of a continuation of the fiscal policy adopted in the depression years. Current expenditures were held down, tax rates were kept high and capital expenditures were practically eliminated. Nevertheless the over-all deficit averaged about $2 million per year, and outstanding debt rose from $119 million in 1933 to $125 million in 1936.

The extent to which expenditures were affected by the retrenchment is indicated by the following table:-

$000

	1930	1936	Increase	Decrease
Net Debt Charges	1,782	3,896	2,114	
Relief	498	3,433	2,935	
Public Domain	452	742	290	
Legislation	187	271	84	
Highways	1,416	704		712
Education	2,199	1,552		647
Welfare	3,494	3,054		440
Justice	890	666		224
Government	1,163	998		165
Agriculture	271	162		109
Others	109	71		38
Total Expenditure	12,461	15,549	3,088	

The table emphasises the extent to which expenditures, other than relief and net debt charges, were in 1936 still below the 1930 level. They had been cut by 25% from 1930 to 1933, but in 1936 they were still 19% below the 1930 level. Since 1933 the only service that has shown any substantial recovery has been welfare (old age pensions and medical services).

In the revenue system, the outstanding change was the shift of the emphasis on taxation. By 1936 licences had just recovered to the 1930 level, liquor control was still below the previous level, there had been slight increases in the subsidy and in the domain revenue, but taxes had risen from $5.2 million to $7.9 million, from being 46% of the revenue to almost 56%.

Despite the tax efforts, the reduction of normal expenditures and the cutting of capital expenditures, the province was unable to prevent the steady increase in outstanding debt, even after 1933. The evidences of economic recovery have not been striking, the relief costs have kept fairly stable, and the increases in the liquor and licence revenue indicate only the slow recovery of spending-power in the province.

Between 1930 and 1936 inclusive the Province had expended $15.5 million on direct relief. By 1936 the balance sheet showed $3.1 million as a provincial contribution to the relief works of municipalities, relief advances of $3.9 million to the City of Winnipeg, $3.0 million for relief work on provincial highways, buildings, etc. and $1.2 million advanced to other relief accounts: in all approximately $27 million have been spent for relief purposes by the provincial government. This represents only part of the depression expenditures: the expenditures on the Farm Loans Association, the Co-operative Wheat Producers Ltd. and the exchange losses also represent depression costs. The extent of the deficit financing is indicated in the growth of the province's liabilities to the Dominion, the treasury bills held

by the Dominion having increased by over $20 million since 1930. The treasury bills held by banks also increased, but of the $12.8 million outstanding in 1936, an amount of $7.1 million was held by the Bank of Commerce following its assumption of the liabilities of the Savings Office in 1932, and this was guaranteed by the Dominion government.

Summary

(1) The increase in debt in Manitoba in the 1929-36 period was below that in any other province (Prince Edward Island excepted). This increase was due mainly to relief, and occurred in spite of a severe cutting of ordinary expenditures, and in spite of the existence of a tax system that was comparatively heavy, as compared with other provinces. In addition, the receipt of the Dominion grant concerning the transfer of natural resources has to be considered as a source of revenue that helped to hold down the debt increase during the depression years.

(2) All services (except relief and debt) were in 1936 still below their 1930 level, and capital expenditures were still negligible. The replacement of provincial equipment cannot be unduly deferred.

(3) The tax level was lowered slightly in 1936. To some extent this reduction has to be construed in the light of the changed financial position of the City of Winnipeg under the constant impact of depression. The metropolitan area entered the depression with its own finances in a not unsatisfactory condition, but the fairly constant relief expenditure, and the growth of taxation as a whole (provincial and Dominion) have tended to involve fairly full utilization of its taxable capacity. An increase in the taxable capacity of the City depends primarily on the economic future of the prairie region as a whole, but in view of the changed debt position of

the municipality and of the province, it cannot be assumed that a small recovery would greatly enhance the taxable capacity. The new level of debts and the need for replacement expenditures not merely in physical but in human resources (welfare and education), are likely to absorb whatever revenues would be available after a slight recovery in regional income, and a reduction in relief costs.

Financial Position of Saskatchewan

In Saskatchewan, the main feature of the financial history has been the trebling of the outstanding debt since 1928.(1) In the post-war period, from 1921 to 1928, the province had apparently reached a condition of some equilibrium after its initial formative stage, and the debt was relatively low and stable. The events of the years following 1928 went far to alter that position. Accordingly, in Saskatchewan there are two stages of importance in the financial growth, the first in the formative period of provincial policy, (up to 1921), and the second, and more important, in the drought-depression period after 1928.

The early financial history of the province revealed the influence of factors that were affecting the whole prairie region, but it showed also that the methods of meeting needs in Saskatchewan were in some instances distinctive, and quite different from those adopted in the neighbouring provinces. The frequent reference of debatable matters to the investigations of royal commissions, before the formulation of practical policies, was in contrast to the usual methods adopted in Alberta. The period up to 1908 especially, was one of such intellectual gestation with respect to fundamental policies, although during this initial period, the educational, judicial, and public works requirements of the province were all begun. The appropriate methods of handling the telephone needs, and of the organization of rural communities, were under consideration by commissions, and the need for spreading the railway system was striking enough to merit full government attention. Up to 1908, however, the government managed to meet both current and capital expenditures from the ordinary revenues. By then the scale of government commitments was beginning to be enlarged to the growth of

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(1) In 1928, the outstanding debt was \$63.8 million: in 1936, \$180.5 million.

population, and need for provincial institutions and equipment - roads, buildings, schools, hospitals, etc. The latter requirement alone necessitated some resort to borrowing. There was also growing a clearer formulation of opinion with respect to government investments. At this time, agricultural opinion (as voiced through the Grain Growers' Association) expressed their requirements as (1) seed grain assistance and hail insurance; (2) need for railway extensions, removal of the railway car shortage problem, and consideration of the advantages to be gained from a Hudson Bay Railway; (3) government ownership of elevators; and (4) difficulties of securing credit advances on wheat. Each of these issues became an integral part of provincial interests within the next decade. In 1908, however, the government was concerned mainly with the question of railways and telephones, and with the organization of municipalities.

With respect to the encouragement of railway building, Saskatchewan was in a different position from either Manitoba or Alberta. Manitoba had pushed railway building through the last decade of the 19th Century, and as the west opened under the impetus of capital import and immigration, railway building proceeded westwards. Saskatchewan, finding railway growth steady, but slow, was able to confine its railway policy to the giving of guarantees ($13,000 per mile) to the Canadian Northern and the Grand Trunk Pacific, and although vocal opinion demanded a Hudson Bay Railway, the province regarded that venture as a federal responsibility, and confined its railway policy to guarantees. The policy began in 1908, and later, guarantees were given both for railway building and for construction of terminals in the provincial cities. By 1920, the guarantees amounted to about $28 million. By confining its activities to guarantees, Saskatchewan did not encounter the upthrust of debt that Alberta experienced from its more positive railway policy.

With respect to telephones, in 1907, with the example of Alberta before them, the conservative opposition, the Grain Growers' Association, and the Boards of Trade pressed for government ownership of telephones, while the Union of Municipalities recommended municipal ownership combined with government trunk lines. The commissioner[2] appointed to study the matter recommended government ownership of long distance lines, but thought that the rural service should be left to rural municipalities, with some financial help from the province. These recommendations were embodied in the government legislation, the government undertaking long distance connections, and encouraging rural development by delivery of poles at the nearest railway station. The Rural Telephone Act allowed five or more persons to organize into a co-operative company under the Department. In 1909 the Bell system was purchased, and afterwards the Saskatchewan Telephone Company. Thereafter the system expanded rapidly to meet the spread of settlement and the increase of population, and by 1913, the government investment in telephone plant amounted to $5.4 million, while the capitalization of rural companies probably exceeded $1 million. In 1913 the rural system was reorganized, and rural companies, with the approval of the minister, were allowed to issue debentures to a maximum of $350 per mile, the funds for repayment of these to be raised by a tax on all lands within 100 yards of the line. This method forced the absentee landlord to meet some of the cost, and by securing the independent financing of the rural systems, increased the traffic on the government lines without adding proportionately to the government's expenditure on rural systems. But this same device, by separating part of the actual costs to subscribers in taxation, and by allowing rural systems to borrow, may have encouraged over-expansion in many districts. The great increase in incorporation of rural companies, following the 1913 Act, and the especially

(2) Saskatchewan selected as its commissioner the man who had served as expert before the Select Parliamentary Committee on the telephone question in 1905.

great increase in the rural system following the good 1915 crop, indicated that rural expansion was apt to be rapid so long as the market for telephone debentures was good, despite the rising costs of materials during the War. In the 1917 report of the Telephone department, misgivings over the rapid increase in rural telephones were expressed. In the six years ending April 1919, 32,000 miles of new rural pole line had been constructed, and rural debenture issues exceeded $8 million. In keeping with this expansion, the provincial government had to enlarge its undertakings on capital account.(3) In the post-war boom, after the removal of federal restrictions on debenture issues, the rural system crowded a $7 million expenditure into the 1919-22 period, and again the provincial government had to expand its trunk and exchange systems. By this time, the provincial demand for telephone mileage was almost satisfied, and thereafter it was hoped that while mileage would alter little, subscribers might continue to increase. In 1915 the telephone tax levy was $92,000: in 1922, $1,835,000 for the province as a whole. Thus, although the system as a whole had expanded more rapidly than in the other provinces, the compromise between government and rural co-operative ownership was ensuring a repayment of telephone debentures, and this repayment continued so long as the area was economically stable (i.e., up to 1929, when some 70% of the rural debentures had been repaid).

With respect to elevators, which to many farmers in both Saskatchewan and Manitoba seemed a matter for government ownership, the Saskatchewan government, unlike that of Manitoba, appointed a commission of investigation. This commission recommended co-operation among the farmers, and thought that the government should give financial assistance in the form of mortgage-secured loans for the construction of elevators. In 1911, when the Manitoba government-owned elevators were in difficulties, the Saskatchewan Co-Operative Elevator Company was incorporated, to do all things incidental to

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(3) The government telephone investment rose from $5.4 million in 1913 to $11.2 million in 1921.

the marketing of grain. It had $50 shares, sold only to agriculturalists, who could hold not more than 10 shares. The government was authorized to loan not more than 85% of the cost of company elevators. This company provided competition in the elevator field, just as the Grain Growers' Association did in the 'commission' field, and the government stimulus to railways in the transport field.(4) By 1913, the provincial government had invested $1.3 million in the elevators.

The total assets in the balance sheet in 1913 were as follows:

		Millions of $
Active assets		4.3
Telephones		5.4
Railways (a)		17.9
Buildings		7.4
Roads		4.4
Advances		.8
		40.2
Less Current Surplus	.2	
Capital Surplus and Sinking Fund Reserve	.8	1.0
Outstanding Debt		39.2

(a) Consists of guaranteed issues of the Canadian Northern and Grand Trunk Pacific Railway Companies, later assumed by the Canadian National Railways.

The active assets were mainly cash and the elevator advance. Buildings and roads comprised over half the debt, the buildings covering mainly the new parliamentary building, the university and the hospitals. Some expenditures on building and roads had been met from ordinary revenues in the early years of the administration.

During this period of growth, which was exceptional even for Canada at this time, the revenue system of the provincial government was not broad, or elastic. The municipalities had the exclusive privilege of collecting taxes from real estate, while the provincial revenue system depended largely on the Dominion subsidy, with licences and fees, corporation, and railway taxes

(4) Gradually the outstanding needs of the farmers with respect to organization and transport were being met. The railway policy had still to be completed, and the question of farm credit and interest charges still remained.

making up the balance of the revenues. In 1908 about 70% of the revenues came from the subsidy, but as settlement proceeded rapidly, the other sources of revenue rose, especially after 1910, so that by 1913, the subsidy formed nearer 35% of revenues. The fees increased rapidly during the development period, especially those from land titles, but the railway, corporation, and inheritance taxes together formed only about 5% of the revenues. In 1913, the revenues were as follows:

	Thousands of $ (a)
Subsidy	2,115
Supplementary Revenue Tax	572
Other Taxes	332
Licences	1,778
Sale of Commodities	461
Liquor	218
Other	588
Total Revenue	6,064

(a) 1913: 14 month period.

The dependence of the revenue system on the subsidy and on licences (particularly land titles and law transfer fees) was obvious. The tax system was very simple, with a supplementary revenue tax levied at a flat rate per acre, with some other taxes mainly on corporations, and with an insignificant amount from succession duties.

The ordinary expenditures reflected the growth of the province, particularly after 1908 when debt charges were added to the expenditure system. By 1913, however, net debt charges were still low. At that time, the outstanding single expenditure item was on education, but the amount of the expenditure absorbed by government, justice and highways, indicated the youthfulness of the provincial economy, and its concern with the primary requirements of settlement. In order of importance, the expenditures in 1913 were as follows:-

	Thousands of $ (a)
Government (including justice and legislation)	1,813
Education	1,201
Highways	661
Agriculture	653
Net Debt Charges	482
Welfare	467
Other	358
Total Expenditure	5,635

(a) 1913: 14 month period.

The sudden change in the rate of expansion after 1912, the poor wheat crop in 1914, and the drying up of immigration, all led to considerable contractions in revenue, especially from land fees. Deficits on current account followed.

The expansion of acreage and the good crop of 1915, and the upturn in wheat prices during the War, helped to restore the revenues from fees and from taxes, but even by 1916, the proportion of revenue from taxes (corporation and inheritance) was still very small, amounting to only 7%. In that year, a Patriotic Revenues Act was passed to assist in meeting the new expenses incidental to the War. In the following year, this was superseded by the Public Revenues Act, and the tax raised from one to two mills on the dollar value of all rateable municipal property, with 1 cent per acre on land in the local improvements districts. In this way, the tax became available for general, as distinct from War, expenses. Although the province was adding to its revenue system by this increase, it was not significantly broadening the basis, but was rather adding to the land taxes, and encroaching on the real property taxation hitherto reserved for the municipalities. However, in view of the agricultural nature of the community, any provincial tax had to be near the value of land, or near the income from land. The province at this time took the former in preference to the latter alternative. In 1917 also, the province followed Alberta's example by imposing a tax on wild lands (at rate of 1% of assessed value on lands which owner has not cultivated to a certain degree). This Act repealed the "surtax" on uncultivated land

imposed in 1913 by the Rural Municipality Act. These new taxes (collected for the province by the rural municipalities) increased the proportion of revenues that came from land, and by 1921, these new property taxes alone yielded 33% of revenue. Inheritance and corporation taxes had responded to the war boom, and taxes as a whole produced 42% of the revenue as against 15% in 1913.

Taxation of land was still regarded as the most appropriate form of taxation in Saskatchewan, but the conditions which gave rise to the new land taxes in 1916-18, and the increased burden that resulted from these taxes, both indicated the improbability of finding a steady source of income from this source. The collapse of the land boom after 1912 had shown that steadily rising land values could not always be expected, and the increases of taxes on land (public revenues and wild lands taxes) were becoming sufficiently burdensome to induce some change in public opinion.(5) It was not until depression recurred in 1921-4, that departmental documents (Report of Department of Municipal Affairs, 1923-4, p.8) voiced the changing opinion, and suggested that taxes must be less on land, and more on improvements and on other forms of wealth. The effects of the depression produced the realization that a constant rise in land values was unlikely, and that since certain expenditures (e.g.,debts) were likely to become fixed charges on the budget, new forms of taxation would be necessary.

The entry of the provincial government into the field of taxes on land and on improvements also made the question of the equality of assessment, as between municipalities, an important issue. Municipalities that had formerly had high assessments and low mill rates, tended to have to pay an unduly large share to the province in the new taxes. The need for equalizing the basis of assessment soon roused complaints, and in 1921 a commission was appointed to study equalization. The recommendations were implemented by the Saskatchewan Assessment Commission Act (1922), which

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(5) A surplus in 1920 permitted the government to repeal the older supplementary revenue tax which had been imposed at a flat rate per acre,and had been used in part to make grants to education.

appointed a permanent commission to supervise and equalize assessment, with adjustments to be made from time to time.

In the period after 1916, the new taxes increased the importance of tax revenues, and they took first place as revenue producers, while licences took second. The subsidy fell to fourth place in the War and post-war period.

In 1921, the chief revenues were:

	Thousands of $	Increase over 1913 (a)
Taxes	4,008	3,104
Licences	1,968	190
Subsidy	1,753	-
Total Revenues	9,460	3,396

(a) 1913: 14 month period.

The increase in licences was not great: the expansion of motor licence revenues had been considerable, but it was partly offset by the decline in revenue from land titles and law fees on transfers.

During the War and post-war boom, revenues had tended to keep ahead of expenditures. But expenditures were influenced by rising costs, and by the growing needs of the young community. The expenditures on government, on road, and on welfare, tended to rise quickly. The extension of government activities increased the costs of administration and of maintaining departments. The need for additional roads as settlement spread, the need for road improvement, for enlarged grants for mental and other hospitals, and for mothers' allowances, all tended to push up total expenditures. Net debt charges and education absorbed over 36% of the expenditure. The expenditures, and their changes between 1913 and 1921 are shown in the following table:

	1913 (a)	1921	Increase	Decrease
		Thousands of $		
Education	1,201	2,854	1,653	
Government	1,812	3,127	1,315	
Welfare	467	1,570	1,103	
Net Debt Charges	482	1,243	761	
Highways	661	1,236	575	
Other	359	882	523	
Agriculture	653	602	——	51
Total Revenue	5,635	11,514	5,879	

(a) 14 months.

The education expenditures took a comparatively large part of the total, the Saskatchewan government making larger grants to schools than the other Prairie Provinces. These grants were associated with the land taxes which were raised by the municipalities, and in part returned to them as school grants, a method that tended to distribute education grants according to the needs of school districts rather than their ability to pay.

The gross debt charges had increased more than any other expenditure in the War and post-war years, by reason of the new government commitments, and the increase of $29 million (6) in the direct debt from 1913 to 1921. In 1921, however, Saskatchewan still spent less than 11% of her net expenditure on debt charges (less interest receipts), a proportion that was bettered only by Ontario and Prince Edward Island in that year. The increase in debt between 1913 and 1921 amounted to $14 million, (6) and the balance sheet showed an increased investment of $12.7 million in public works, $10.6 million in advances, $5.8 million in telephones and $5.3 million in active assets, the bulk of the latter being an increase in inventories and taxes receivable. The increase in telephone investment during the War period has already been mentioned. The increase in public works went largely to hospitals ($4.4 million), to government buildings ($2 million), to highways ($3.9 million), to the university ($1.2 million), and to relief works on

(6) From 1913 to 1921 direct debt increased by $29 million while the indirect debt decreased by $15 million due largely to the assumption of $18 million guaranteed bonds of the Canadian Northern and Grand Trunk Pacific by the Canadian National Railway Company.

highways during the post-war depression ($1.1 million). Relief accounts ($2.0 million) also helped to account for the $10.6 million increase in advances, as shown in the balance sheets between 1913 and 1921. But the main reason for the increase in advances arose out of the establishment of the Farm Loan Board. By 1921, $7.9 million had been advanced to the Board, and $1.0 million to the Co-operative Creameries. The extension of government activities in these agricultural undertakings had been hastened by the breaking of the pre-war boom after 1912. The resultant depression led to demands for government assistance in different directions, and in 1913 Saskatchewan had a "commission year". One commission studied the feasibility of diverting the waters of the South Saskatchewan river to supply water and power to the province: the drought question was already under consideration. Another commission studied the local government situation, the municipalities feeling the effects of tightness in the financial markets. The Board of Highway Commissioners was under review in order to adapt it to the new road needs of the province. And most important of all were the agricultural commissions, one studying hail insurance, and another studying the wheat markets and the ways of establishing agricultural credit. This involved not only a study of European markets, but also of European methods of agricultural aid, land banks, etc. The breaking of the boom was turning attention to one of the fundamental farming difficulties, others concerning transport, elevators, seed grain assistance, etc., all having been tackled in greater or lesser degree in the pre-war period. The question of markets and of credit remained for initial consideration. With respect to markets, nothing very positive could be done by the prairie governments (apart from the work already done to aid internal transport, grading of the product, etc.), but with respect to credit, the commission found that Saskatchewan farmers already had to pay interest on their private debt of $150 million ($65 to mortgage companies, $50 for land purchases, and $40 for machinery). The growth of this debt had been associated with the pre-war boom, but the boom had not created conditions that permitted full repayment of the debt. The question that confronted

this commission appears to be fundamental to agricultural regions, and in Saskatchewan several circumstances characterized the debt position. (1) The pre-war boom had been part cause, and part effect, of the private borrowing (and also of the government borrowing and debt guarantees). (2) The boom enlarged wheat output and helped to stop the price rise, from 1909 onwards the Liverpool price tending to alter its trend, until rocketted upwards again by war shortages. (3) The debt associated with the boom, both agricultural and governmental debt, was difficult to adjust downwards, partly because the purposes to which the loans were devoted did not always yield returns adequate to permit their repayment, and partly because agriculturists (and governments), unlike joint stock companies, cannot secure a large part of their capitalization from ordinary equity shares, but have to resort to fixed interest loans. In times of falling income, these fixed charges become relatively heavy, and may provoke further debt growth.

To meet some of these difficulties, and to help to reduce the interest charges to farmers, the Farm Loan Board was established in Saskatchewan in 1917, to make loans to farmers. In 1918, 80% of the interest due to the Board was collected, but in the 1921 depression only 37% was collected. It appeared as if private loans were being repaid first, and government loan payments postponed. The effect of the 1921 depression on the Farm Loan Board was perhaps inevitable, irrespective of the particular details of its policy. In Saskatchewan, the Board had aimed at lending in new districts, and at establishing new farmers. These people had little time to establish themselves when the war boom broke, and so the interest arrears seemed comparatively high in the 1921 depression. The Board, however, had entered into competition with the mortgage companies, and the effect of this competition on interest charges generally may be the measure of the Board's work, rather than its own accounting position.

Despite the provincial debt growth between 1913 and 1921, it was still much below that of the neighbouring provinces. On a per head basis, in 1921, the debt was only about half of that in the neighbouring provinces, and the scale of taxation reflected that fact. The smallness of the public debt charges moreover, permitted the province to distribute its ordinary revenues with more emphasis on education and public health than in the other Prairie Provinces, the welfare services having increased comparatively rapidly in the previous few years, with the grants to mental and other hospitals, and with the introduction of mothers' allowances. Education grants to schools and to the university had also expanded.

The period up to 1924 was not one of prosperity, although wheat acreage kept near its 1921 peak, and rose to a new peak in 1925. Agricultural income fell sharply in 1921, and although it recovered somewhat, it did not establish a new upward surge until 1925. The economy was marking time, and making readjustments to the conditions created in the short post-war boom. The government aided this policy of readjustment in so far as it announced its aim of trying to maintain the revenue system unchanged, and of trying to abstain from those taxes on income and property that were being contemplated or adopted in the other western provinces. This aim, however, could be fulfilled only by rigorous control over ordinary and capital expenditures, and this retrenchment was undertaken throughout the period to 1925. The rate and the amount of debt growth from 1921-26 was smaller than in any other province (Prince Edward Island excepted). Capital expenditures were cut in 1922, and maintained low. Ordinary controllable expenditures were also cut, but the rising costs of education and public welfare were making it difficult to keep expenditures in line with revenues that were not particularly buoyant. The construction industry kept low throughout the period, as compared with its 1921 level, when telephone and other government and business construction had been at their post-war boom peak. The ordinary expenditures were kept down until 1925, legislation, attorney-general's department, public

works, highways, and agriculture, all being subject to curtailment. In that year, which was a good agricultural year, some expenditures rose, particularly on education, public works, and public health.

By 1925, the increase in debt over 1921 was only $5 million, and the outstanding debt stood at $58.1 million. Almost all the debt increase had been involved for public works, particularly highways.

Gross agricultural income rose sharply in 1925. It reached a peak in that year and kept high and fairly stable right through 1928. This degree of prosperity gradually broke through the policy of retrenchment that had characterized government expenditures in the post-war depression. The rise in agricultural income increased the desire for new government services, while the same prosperity, by increasing the buoyancy of revenues, seemed likely to provide the revenues for meeting new services. Under the impact of the boom, therefore, both current and capital expenditures expanded, and the province was just reaching new high levels of expenditure when the depression came. The following table shows the growth of the over-all deficit in the boom period:

	1925	1926	1927	1928	1929
	Thousands of $				
Revenue	12,411	12,782	13,273	15,694	14,048
Expenditure	11,045	11,098	11,551	14,509	16,398
Surplus	1,366	1,684	1,722	1,185	-2,350
Capital Expenditure	1,487	1,614	2,379	3,710	8,935
Over-all Deficit (-) or Surplus (+)	- 121	+ 70	- 657	- 2,525	-11,285

It was not until 1927 that the capital expenditures began to move ahead. Up until then the current surplus had been fairly stable, but it fell in 1928, and in 1929, when revenue fell and expenditures increased, there arose a fairly large current deficit, and this coincided with larger capital expenditures for highways, hospitals, and the newly created power commission. In 1930 these capital expenditures on public works continued to increase, and they

coincided with growing relief expenses, so that capital expenditures rose from $8.9 million in 1929 to $14.3 million in 1930, and debt which had risen by $12.6 million in 1929 rose by another $23.2 million in 1930. The debts of the provinces as a whole rose fairly steadily from 1926 to 1929, but Saskatchewan's contribution to the annual rise was only 1.8% in 1926, whereas in 1929 20% of the total provincial debt growth in that year was due to Saskatchewan.

In Saskatchewan, the total revenues rose in the boom years (1925 to 1928) but the rise was concentrated on a few revenue items. The revenue rose from $12.4 million to $15.7 million, but this rise of over $3 million came mainly from liquor profits ($1.2 million), licences, particularly motor licences ($1 million), and taxes ($0.6 million). The rise in tax revenues was slight, considering the new levels of agricultural income. The revenue adjustments during these years did little to take advantage of the buoyant agricultural income. The taxes on real property had been the major revenue producer in 1925 (25% of total revenue), but their yield declined, and by 1928 they yielded only 14% of revenue. Following the entry of the province into liquor control in 1925, and following the improved fiscal position, the Public Revenue tax was reduced from 2 to 1½ mills. The government was then (1927) under pressure from the municipalities, asking for a share of the liquor profits, which the province had intended for debt redemption. Instead of meeting this request, the government lowered the public revenue tax, and decided that only 10% of liquor profits should be earmarked for debt reduction. At this time most of the municipalities were in a comparatively healthy position; the arrears of taxation being reduced as well as their debts. The reduction of the tax, and the size of the educational grants from the province combined to put the Saskatchewan municipalities in a more favourable fiscal position than many other western municipalities, and from 1927 the municipalities devoted larger expenditures to public works, particularly highways (in line with provincial policy). There were, however, wide variations in the needs, and the taxable capacities

of the municipalities in different parts of the province, and these variations were liable to be revealed if general income (or sectional incomes) moved downwards. But up to 1928, the rate of debt reduction and the reduction of the tax rates all indicated a situation of financial fortune.

The only significant change in the provincial revenue system was the adoption of the gasoline tax in 1928 [7] and this was associated with the new upward direction of debt taken in that year. Demands for improvement of the highway system were becoming insistent, and the economic and financial position of the provincial government seemed to suggest that the time was ripe for highway improvement. The three years (1926-28) had produced the most stable total agricultural incomes in the history of the province; building (including railways) was active, and secondary industries (packing and milling) were expanding. Between 1926 and 1929 ordinary expenditures rose, the rise becoming steep in the later stage of the boom. Between 1926 and 1930, welfare, excluding relief, had risen by $1.7 million, largely for old age pensions, education by $1 million, net debt charges by $1.1 million, highways by $0.9 million, and in addition by 1930 relief charges were beginning.

As a result of the growth of capital and current expenditures, the Saskatchewan provincial government entered the drought-depression period with many new commitments. To some extent these commitments had arisen out of Saskatchewan's previous "economy" in expenditures, and they might be in large part regarded as the fulfilment of needs that had been postponed in Saskatchewan while they had been carried out steadily in other provinces. The effect of these commitments and the emergence of the drought-depression factors affected the financial position as follows:

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(7) Saskatchewan was the last province to impose a gasoline tax,

	1929	1930	1931	
	Thousands of $			
Revenue	14,048	13,307	10,066	
Expenditure	16,398	19,059	28,291	(a)
Current Deficit	2,350	5,752	18,225	
Capital Expenditures	8,935	14,265	5,437	
Over-all Deficit	11,285	20,017	23,662	(a)
Debt Increase	12,583	23,227	37,914	(a)

(a) Includes $5,339 of relief expenditures subsequently assumed by the Dominion.

As a result of these changes, debt rose from $63.8 million in 1928 to $137.6 million in 1931, an increase of 115%.

It will be noted that in 1931 the debt increase ($37.9 million) far exceeded the over-all deficit. The difference was due to the necessity of implementing the province's wheat pool guarantee ($13.3 million) in that year.

The above table indicates the circumstances that surrounded Saskatchewan's transition from an apparently sound economic and financial position into one that was considerably less so. The main characteristics were the fall in revenue, the rise in expenditures and deficits, and the cutting of capital expenditure after 1930. These characteristics may be regarded in some detail.

(1) The fall in revenue was as much as 28% between 1929 and 1931. During this period there was little change in the revenue system, except for an increase in the gasoline tax (2 cents). The largest fall was in the liquor profits ($1.5 million), the second in licences ($1.4 million), and the third in taxes ($1.1 million). The fall in property taxes, in motor licences, and gasoline taxes (1930 to 1931), along with the fall in liquor profits, was evidence of the great contraction in agricultural income, as the drought and the depression combined to reduce spending power and taxable capacity. Nevertheless, some new revenue efforts were made in 1931-32; the public revenue tax was raised, the gasoline tax again raised,

motor licences increased, corporation taxes on banks, insurance, trust and mortgage companies increased, and an income tax introduced with a low exemption. The effect of these taxes was to raise total revenues by 20% between 1931 and 1932, just when the cash income of agriculture was being forced towards what seemed to be a minimum. And despite the low level of net agricultural income in 1932 and 1933, the revenue then raised was only 23% below the revenue raised in 1928, the peak year of agricultural income in the province.

(2) The rise in current expenditure between 1929 and 1931 was from $16.4 million to $28.3 million, an increase of $11.9 million. Relief charges alone had accounted for almost all the increase. Net debt charges had increased by $2.4 million, and education and other welfare had increased. But these smaller increases had been approximately balanced by the reductions on highways expenditures ($1.5 million), and the cuts in expenditures on legislation, justice, agriculture, etc. The main reductions in expenditure, like the main increases in taxes, were not evident until the following year (1932), when every service (except net debt charges) was lowered. In short, current expenditures on education, welfare, general government, etc., tended to continue increasing right into 1930, some were reduced in 1931, and all (except net debt) were reduced in 1932. With the cut in 1932, and with the increased taxation, the current deficit, which had reached a peak of $18.2 million in 1931, was reduced to $8.5 million in 1932.

(3) The capital expenditures, like the ordinary current expenditures rose to a peak in 1930. Then they fell from $14.3 million in 1930, to $5.4 million in 1931, and in 1932 there were no capital expenditures. The peak in 1930 had been due mainly to highway building ($7.3 million), to advances to the Farm Loan Board ($2.5 million), to other public and relief works ($1.6 million), and to relief accounts ($2.8 million). The over-all deficit reached $20 million in 1930, and with the advances to the power commission ($3.3 million) the debt rose by over $23 million in that year.
In 1931, however, the highway and other works

were cut to negligible levels, and the $5.4 million spent on capital works in that year went mainly to relief works and the Farm Loan Board. By 1932 these were also cut, and capital expenditures may be said to have ceased, not to be restored until 1935 when they reached $2.2 million.

The history of the years from 1929 to 1932 went far to change the whole financial position of the province. The fall in prices, and fall in yields both contributed to the changed economic position. In such conditions, the financial history of Saskatchewan after 1929 is really the history of an attempt to finance widespread relief in a province where there were no large reserves of private wealth. In these conditions, considerable support from the Dominion government was necessary, both directly, and indirectly through assistance to the province in financing its share of special expenditures.

During each of the years from 1929 to 1936, the drought and the depression factors shifted their relative importance as determinants of the economic and financial position. In 1929, the drought factor caused a fall in income, which fall was smaller than it would have been had wheat prices not kept up. In 1930, however, the yield was higher than in the previous year, but the wheat price had fallen by over 50%, so that agricultural income was pushed down further. In 1931, both price and yield were lower, so that income fell still further. In 1932, however, the yield was much better, but price touched bottom, so that income improved little. From 1933 to 1936 price improved fairly steadily, but yields kept low, so that the recovery of agricultural income as a whole from the low point of 1931 has not been encouraging.

It seems clear that even if there had been no drought, the depression would have caused a serious dislocation in the economic and financial position; and the price recovery after 1932 might have been smaller than it in fact was, had drought not kept down the supplies of Canadian wheat. But with drought added to depression, the question of feed became more difficult, and the

cessation of production in the drought region led to intense economic disturbance to households, and to the necessity for increased relief charges. Thus the total relief expenditure (Dominion, provincial and municipal) did not ease with the recovery in prices after 1932, but increased according to the ravage of the drought, being particularly high in 1934, and only a little less so in 1935. The relief expenditures of the government of the province were as follows:

	1931	1932	1933	1934	1935	1936
			Thousands of $			
Direct Relief, Agricultural Relief and Public Works, Provincial Share and advances to Municipalities	15,833	5,567	6,135	18,864	13,137	10,874
Less: Proposed Dominion write-off of Relief Loans (a)	5,339	643	2,239	14,164	3,746	549
	10,494	4,924	3,896	4,700	9,391	10,325

(a) Proposed Dominion write-off of relief loans, $5,998 in 1934, $3,000 in 1935, and $17,682 in 1937-38 applied retroactively to years in which expenditures were incurred.

The above total for relief during these years amounted to approximately $70 million,(8) and in 1936 the treasury bills held by the Dominion government reached $63.4 million. Of this amount the proposed write-off is $26.7 million.

The increase in outstanding debt from $99.6 million in 1930 to $180.5 million in 1936 was attributable almost entirely to the depression-drought circumstances, by far the major part of the cost being represented by direct relief, and the remainder by the wheat pool guarantee, the relief works, the seed grain and other relief loans of the province. But the full extent of the depression effect is not evident by consideration only of the relief payments. The failure to maintain capital works will lead to future provincial expenditures on replacement: the cutting of ordinary expenditures may have somewhat similar repercussions.

(8) The total revenues of these years amounted to $73 million so that relief payments alone were equivalent to over 96% of the total revenues through this period.

The change in the ordinary expenditures between 1930 and 1936 is worthy of note:

	1930	1936	Increase	Decrease
			$000	
Relief	1,633	7,439	5,806	
Net Debt Charges	2,842	5,758	2,916	
Welfare	3,482	3,355		127
Education	4,257	2,841		1,416
Highways	2,076	920		1,156
Government	3,135	2,578		557
Other	1,634	1,104		530
Total	19,059	23,995	4,936	

In view of the fact that 1936 was among the most favourable of the financial years after 1930, with relief charges well below the 1934 level, and with some expansion in welfare, education, government and highway expenditures, the above table does not indicate the full extent to which the provincial expenditure system had been directed at relief financing, but even in 1936, the domination of the relief financing is unmistakeable, the relief and net debt charges absorbing 55% of the total expenditures.

The level of the agricultural income in Saskatchewan severely limited the taxable resources of the region. New revenue efforts were made in 1932 by an increase in the public revenue tax, in gasoline and motor licences, in corporation taxes and in the imposition of an income tax. An increase in the gasoline tax was made again in 1935. As a result of these measures, the tax system has changed somewhat from the relatively simple system that existed in the boom days. But since corporations are few, these taxes are not lucrative, and since private incomes are not high, and are fairly evenly distributed, there is little to be expected from income taxes and inheritance taxes at present. For these reasons, the change in the tax system from 1932 onwards has increased only slightly the importance of taxation in the revenue system. In 1928, when revenues equalled $15.7 million, taxes yielded 31% of that total. By 1936, when revenues were $14.0 million, taxes yielded only 40% of the total. The significant

changes in the production of revenue between 1928 and 1936 were as follows:

	Increase	Decrease
	$000	
Taxes	811	
Licences		1,147
Liquor Control		1,645

The increase in the taxation was small, therefore, and was attributable mainly to gasoline, and partly to the income and corporation taxes. The decline in licences came largely from the fall in motor licences. This fall, and that in liquor profits, are indicative of the contraction of spending power in the province.

SUMMARY

(1) The financial position in Saskatchewan has to be considered mainly in terms of the events that have occurred since 1929. Since then, debt has risen 136% to the 1936 level of $181 million. But revenues in 1936 which amounted to $14 million were 11% below the 1928 level. Net debt charges alone were $5.8 million in 1936, and relief $7.4 million. Together they equalled 94% of the revenues.

(2) A rise in revenues at the disposal of the province is dependent almost entirely on a rise in agricultural income. And it cannot be assumed that a small rise in agricultural income will necessarily increase the taxable capacity. The depreciation of equipment in households and farms has to be allowed for, and so also have the increased private debts. A small rise in agricultural income would presumably serve these purposes, and do little to increase taxable capacity. Government equipment has also deteriorated and any reduction in relief charges, or any slight increase in government revenues, would presumably go to the renewal of services that have been excessively reduced.

(3) But the drought, and the depression have led to certain conditions that may render difficult an improvement in the financial position. The depression induced certain changes of agricultural policy in the wheat importing countries. Wheat yields were rising in Europe before the depression occurred. The depression served to encourage greater self-sufficiency in some importing countries, while later events have induced some to put their agriculture on to a war-economy basis. In such conditions, their desire for imports, now and for some time ahead, is not dependent mainly on the price or the quality of the wheat offered by exporting countries. The drought also produced certain long-term charges, this time affecting the supply of Saskatchewan wheat. The productivity of certain areas within the province has been affected and even given a good wheat market, certain expenses of rehabilitation may be necessary before any rise in income can be secured in these areas.

Financial Position of Alberta

The economic and financial position of Alberta in the last three decades has been influenced by factors that were common to the other Prairie Provinces - the significant rise in world prices from 1896 to 1913, the flow of labour and capital into the region in the boom years, the rapid scattering of settlement, and the concomitant transport and institutional construction. While these conditions and characteristics affected the financial position of the prairie region as a whole, each province within that region encountered its own peculiar needs for expansion, and pursued its own methods of development accordingly. The special conditions that dominated the financial history of Alberta might be summarized as follows:-

(1) Alberta was the last virgin frontier to be settled, and many of the settlers were trained in the technique of exploitation. Many of them possessed capital of their own, and were familiar with American standards of living. And originally they were racially somewhat more homogeneous than the Saskatchewan population, so that the initial demand on the Alberta government for a rapid extension of settlement equipment (railways, roads, telephones, and institutions) tended to be stronger and more insistent than in the neighbouring province. Given this demand, and the ready supply of capital, the main conditions for rapid settlement were present.

(2) Rapid settlement could be achieved only by the provision of an adequate system of transport and communication.

With respect to road-making, the nature of the country tended to raise highway costs above those in the other Prairie Provinces, because of the special needs in levelling, grading and bridging. In addition, the haphazard method of settlement, and the spreading of settlement, involved Alberta

in higher costs for the construction of roads across its wide, barren areas.

With respect to railways, certain underlying circumstances tended to make the railway question in Alberta a more pressing one than in the other Prairie Provinces. For two decades, settlement in Alberta was confined to the narrow belt contiguous to the Canadian Pacific Railway, and to its branches northward to Edmonton and southward to Macleod. Even by 1911, Alberta still had a comparatively large section of its occupied territory far removed from railways, whereas by that time only the west, and south-west parts of Saskatchewan were in that position. Furthermore, with the knowledge of available good lands in northern Alberta, settlement was tending in that direction, and the opening of that area of the province depended on its accessibility to railroads. And lastly, Alberta was at the peak of the transcontinental freight costs, so that competition in railway transport was a relatively important factor, from the point of view of the export possibilities of the province. Accordingly, whereas conditions in Saskatchewan allowed the provincial government to confine its railway policy to the giving of guarantees, in Alberta the desire for rapid settlement, and the special transport needs, led the provincial government into a more ambitious railway policy, begun after 1909, and aimed at the building of railways in the more northerly parts.

With respect to other communications, particularly the provision of telephones, somewhat the same factors prevailed. Immediate connections were required, and in contrast to the highly competitive low-price telephone service south of the border, the Bell system in Alberta held a monopoly, and was unwilling to provide lines into areas that appeared unprofitable, i.e., into villages or thinly settled communities. The resentment of the west on these matters was voiced in 1905 before the Select Parliamentary Committee that considered the methods of furnishing telephones. When the Province of Alberta was

established, the policy of government ownership of telephones was immediately pursued, without opposition. Construction of long-distance lines began in 1906, with little preliminary inquiry or consultation with technical experts. The rapidity of government activity in this "union of the province with cords of copper" was not unrelated to the way in which the growing population was spreading itself over the territories.

(3) The population of Alberta was, and still is, spread more unevenly than that of Saskatchewan or Manitoba. From this point of view, Alberta is the newest, or youngest, of the Prairie Provinces. This distribution, and the movement of the population within the province, affected the needs of the province in utilities and in institutions, and thereby affected the total costs of the extensive equipment required for settlement, making it comparatively high per head of the population.

(4) Since rapid expansion was desired in Alberta, the province undertook, so far as it could, the policies constitutionally open to provinces, namely the guaranteeing, or the direct provision, of equipment in railways, roads, and institutions. In the provision of certain services (e.g., telephones, and social services) Alberta has tended to be an innovator among Canadian provinces.

The policy of provision of equipment in a new area, even if it is carried out with all the technical efficiency and foresight at the government's command, is open to not inconsiderable risks of error. And if the policy has to be fulfilled in a short time, the dangers of error in the spatial or economic distribution of equipment are increased. Furthermore new techniques may emerge to compete out the old ones, as in the case of road transport versus railways in certain areas. The chances of encountering high rates of depreciation on government investments in new areas are, therefore, great, and so far as that depreciation is encountered, the government is

left with deadweight debt. The more the government of a new province is involved in capital expenditure on utilities, roads, and institutions, the greater is the possibility of a part of its debt being deadweight; and if the region is subject to severe cyclical forces which affect its economic structure, the greater the chances of a comparatively large part of the debt being deadweight.

In the period before the War, so great was the rate of economic expansion that almost any government investment in equipment seemed soon to justify itself. (The measure of success in such investments in a new country is not their immediate return to the government in revenue terms, but rather their ability to expedite private investment in provincial resources, which in turn, will tend to increase the population and the revenues of the province. If private development proceeds as is hoped for, the government investment may prove self-sustaining, or even revenue-producing).

As a result of the operation of the factors discussed above, the outstanding debt in Alberta tended to rise more quickly than in the other new provinces. By 1913, Alberta's outstanding debt was $52.1 million, while Saskatchewan's was $39.2 million: between 1913 and 1921 Alberta's debt rose by a further $44 million, while Saskatchewan's rose by $14 million. By 1913 Alberta had a direct investment of $14.7 million in railways whereas Saskatchewan had made no direct investment: Alberta had spent $7.5 million on telephones as against $5.4 in Saskatchewan: but on public works, Alberta had spent only $9.3 million as against $11.9 million in Saskatchewan. By 1921, however, Alberta had overtaken Saskatchewan in its public works, had spent four times more on its utilities, but lagged behind Saskatchewan in its expenditures on agricultural "investments", Alberta having no Farm Loan Board. It was its expenditure on railways in particular that caused Alberta's debt to be above that of Saskatchewan at this period.

Some consideration may be given to the particular factors that contributed to Alberta's debt growth in the pre-war and War periods.

Alberta's developmental expenditures began in 1906 with a modest vote to construct long-distance telephone lines. This equipment was expected to improve communications, speed up colonization, and thereby provide returns that would expand and would later be adequate to cover the telephone costs. Competition with the Bell Telephone system led to its purchase, and new construction was also pushed ahead to expedite the completion of the system. By 1913, when economic recession was beginning to reveal its effects, the government's telephone investment exceeded $7.5 million. During the recession, telephone development slackened, but with the War and post-war booms, additional investment was made. By 1919, deferred costs of maintenance had to be met, and the rates, which were lower than those in Saskatchewan and Manitoba, were raised by one-third. A special investigation was made of the system, and it was concluded that it had suffered from the burden of high costs. These had been inflated by the shifting of settlers and the emergence of unused capacity, by the fixity of charges in face of the increase in prices and costs during the War, and by the failure to set up proper depreciation reserves and proper accounting methods. The report recommended that exchange rates be raised by 20%, toll rates by 25%, and rural rates by 100%; or that a telephone tax be considered.

The only recommendation to be fully implemented concerned the necessary improvement in accounting methods. By 1921, the government investment in telephones approximated $20 million, as against $11 million in Saskatchewan.

The policy of railway investment began in 1909, with a guarantee of $7.4 million of bonds of the Alberta and Great Waterways Railway. This guarantee was intended to assist railway building in the northern part of the province, but as

a policy, this did not receive the same popular support as did the telephone investments, this line in particular appearing to have only remote potentialities of productivity, since the area to be tapped by it was still largely unknown. An almost equivalent guarantee ($7.0 million) was given to the Edmonton, Dunvegan, and British Columbia Railway, and a small one to the Lacombe and North-Western Railway. When the boom broke in 1913, these lines were at various stages towards the process of completion, the Alberta and Great Waterways line commencing operations in 1916. By 1920, the province had assumed the management of this line, having been called on to pay defaulted interest, and to make capital advances. By 1921, $3.4 million had been advanced to this line. By then also, $2.9 million had been advanced to the Edmonton, Dunvegan and British Columbia line, $2.3 million to the Central Canada Railway, just under $1 million to the Lacombe and North-Western Railway, and $155,000 to the Grand Trunk Pacific. In all, capital advances to railways reached $9.8 million, and the total government railway investment was $26.9 million. By 1921, railways and telephones accounted for $46.7 million in an outstanding debt of $95.8 million. The amounts advanced to railways were to expand by another 39% before the railways were sold in 1928-9. But in 1921, the railway construction was not yet completed: it was hoped that the post-war depression was only a temporary sag in the upward incline of long-term progress, that the existence of good lands in the north would attract the next wave of immigration, and would therefore help to justify the railway expenditures.

After utilities, public works were the main contributor to the rise in outstanding debt during the War. Between 1913 and 1921, the investment in works expanded as follows:

	$ million
Public Buildings	4.5
University	4.0
Highways, Bridges	5.8
Irrigation	6.0
Others	.6
Total increase	20.9

The largest single item accounting for the increase was irrigation. The dry years towards the close of the War involved the province in this outlay, which even on the basis of optimistic expectations, seemed unlikely to be of more than narrow municipal significance. It was directed at areas that had been opened by the Dominion government in the pre-war years, and the size of the works, having regard to the populations resident, were comparatively large. In 1921, a full provincial guarantee was given to bond issues for such purposes, the largest scheme being the Lethbridge Northern Listrict, with a $5.4 million bond issue. Additional populations in these districts appeared to be necessary to justify these works, and at a later date additional costs were involved for that purpose.

The drought years at the end of the War involved the province in other guarantees with respect to Seed Grain, Relief and Livestock Encouragement advances, and Hail Insurance. The Alberta loans involved in these projects amounted to over $7 million by 1921,[1] and only a small part of this sum was repaid.

In conclusion, it can be said that in 1921 the policy of rapid development was already involving the province in comparatively heavy charges, and that this was reflecting itself in the relative inflexibility of a large portion of the ordinary expenditures. The telephone undertaking was almost completed, but the railroad work had still to be finished. If the rate of economic expansion proceeded as in the pre-war years, these policies seemed likely to round off the expansion. A continuance

(1) Seed grain and relief $4.6 million: Hail Insurance Board $1.2 million: Livestock Encouragement Act $1.4 million.

of prosperous conditions might permit the provincial government to share in the returns, and to reduce, or repay, the loans that had been incurred to expedite the expansion. On the other hand, if the rate of development slowed down, the costs and the burden of debt on the province would be comparatively heavy, and the deadweight debt would be great or small according to the extent of difference between the realized and the expected conditions. And if actual decline occurred in any areas, not only would the equipment there be used unproductively, but in addition, the province might be involved in new costs of relief, and so far as these could not be met from the ordinary budget, further debts might be incurred. Given rapid economic development, then appropriate provincial action could make considerable readjustments in the debt position: given economic decline, or even stability, provincial action could do little more than improve the technical position of the debt, e.g., by raising sinking fund provisions, and by altering the existent policy of selling savings certificates payable on demand without having adequate reserves, and by ensuring as broad a revenue basis as was compatible with the economic position.

As a result of Alberta's capital commitments, net debt charges by 1921 were already forming 24% of the expenditure. In Saskatchewan, only 11% went to debt charges at this time, and since the total expenditures of the two provinces were then about equal, it followed that Saskatchewan was able to devote larger amounts to welfare, education, and highways, than was Alberta. In view of the change in social psychology, and in view of the demand for highways in the post-war period, it was unlikely that Alberta would lag behind Saskatchewan in the provision of social services, and in the highway expenditures. In short, it was likely that Alberta's current expenditure would tend to exceed Saskatchewan's by the excess of the debt

charges. By 1927, Alberta spent $9.6 million on expenditures other than debt, and Saskatchewan $9.8 million. The higher total expenditure in Alberta in that year was attributable to its debt position. In 1928, the debt charges were lowered somewhat by the sale of the railways.

The growth of Alberta's expenditures between 1913 and 1921 was mainly attributable to the debt growth, but education and welfare combined to add almost as much to the total. Debt, welfare, and education accounted for 69% of the increase. Government (including justice and legislation) accounted for another 20%, and the remainder went mainly to highways. The expenditures were as follows:

	1913	1921	Increase
	Thousands of $		
Debt Charges	563	2,599	2,036
Welfare	270	1,274	1,004
Education	731	2,314	1,583
Justice	503	1,188	685
Legislation	368	500	132
Government	835	1,356	521
Agriculture	330	420	90
Public Domain	81	121	40
Highways	82	839	757
Other	392	205	-187
Total	4,155	10,815	6,660

The distribution of ordinary expenditure was therefore tending more and more to services that were relatively difficult to adjust downwards - net debt charges, social and education charges, which by 1921 accounted for more than half the total expenditures. By then, government and legislation, also something of the nature of an overhead in a budget, accounted for 28%, so that remaining services received comparatively little, highways only 8%. With this growth in the amount of comparatively inflexible expenditure, there was need for a revenue system that would at least yield somewhat stable totals, and would, if necessary, prove elastic. A system to achieve both these ends was difficult to find, even with gradual adaptation. The original revenue system,

established with the province, did contain stability, the Dominion subsidy up to 1910 forming over 50% of the revenues. But the growth of the Dominion subsidy could not, in view of the expenditure growth, provide adequate elasticity. And the attempt of the province to adjust its other revenues was not entirely successful, partly because the necessary broadening of the tax base was only slowly achieved, and partly because almost any tax, or group of taxes, would be sensitive to some extent, to any change in agricultural income. The lag in adjusting the tax base was evident up to 1913. The original revenue system comprised the subsidy (over 50%), fees, fines, etc. (about 33%), corporation taxes, succession duties, railway and education taxes (about 10%). By 1909 it was clear that this system could not cope with the growing expenditures, and deficits continued till 1912, when the new automobile licences, and increased education tax returns sufficed to yield a small surplus. Then in 1913 the tax base was broadened, by receipt of the new unearned increment tax, and in the following year by receipts for new taxes on wild lands, timber areas, education tax on leased land, and amusement tax. But unfortunately they were all imposed, just when the land boom was beginning to deflate. This made evident to Alberta (as it did to Saskatchewan) that revenues were closely dependent on the level of agricultural income, the fall in revenues from 1914 to 1917 reflecting the agricultural conditions of that period. The fact that the Alberta revenues fell less than those of Saskatchewan during this period was partly attributable to Alberta's attempt to broaden its tax base in 1913. This did not indicate, however, that a province subject to wide fluctuations in the main producers' incomes could always meet falling revenues by increased taxes (or new taxes). Apart from the question of the wisdom of increasing taxes in depression, this 1914-17 experience indicated rather that there was some advantage to

a province, subject to wide fluctuations in income, in having some unused taxable sources to fall back on in depression. But if the normal expenditure level tended to absorb most available sources, then this "slack" would not be available. This question was not important in 1914, but it was very important in the recent depression, not only by reason of the great fall in agricultural income in that depression, but equally important, because of the gradual utilization of many of the revenue sources in the period from the War to the depression. At this point in the inquiry, it need only be indicated that the addition to Alberta's tax base in 1913 was not sufficient to prevent a fall in revenue, and a recurrence of deficits. In 1918, additional breadth was given to the revenues by the returns from the new supplementary revenue tax, and by the new coal mine owners' tax. These changes, coupled with the agricultural revival after 1918 that increased returns for all land taxes, were sufficient to yield budgetary surpluses until 1921. By then revenues were almost twice their 1913 level: the Dominion subsidy accounted for only 20% of revenues, and the taxes on real property (land taxes, wild land tax, unearned increment, and supplementary revenue tax) accounted for 25% of revenue as against 2% in 1913. This change measured the broadening of the tax base, but in so far as this part of the base lay directly on land values, which were subject to extreme fluctuation, and in so far as the expenditures were becoming increasingly inflexible, it was clear that this great dependence on land taxes would have to be replaced by dependence on a more diversified revenue system, so far as that could be found. By 1921, however, Saskatchewan was receiving more of its revenue from taxation than was Alberta, particularly from the taxes on land and improvements. And the tendency for Alberta's expenditures to outrun its revenues added considerably to its accumulated current

deficit. The depression in 1921, and the government commitments, particularly with respect to utilities, led to a considerable increase in outstanding debt in that year, an increase of $25 million.

The depression that set in during the latter part of 1920 was particularly unfortunate both for producers and for the provincial government. Because it was world-wide, it was not thought to have any particular connection with the great increase in wheat acreage and farm mechanization in Canada, and so the possibility that new agricultural methods, and new output, might tend to glut future markets was not fully realized. And because there had been abnormally low wheat yields for 1916-1920, the effects of the agricultural revolution had been hidden. When these effects did reveal themselves with the improved yields of 1922 and 1923, the low prices were attributed almost entirely to the depression. And it was particularly unfortunate that the depression occurred just after a series of agricultural innovations, because it reduced the possibility of clearing off the private debt incurred on machinery. Private overhead became burdensome, and there was less opportunity for the government to widen its tax base in such conditions, and a series of deficits ran through the period until 1924. The agricultural depression reduced the provincial revenues, especially since they were largely based on land taxes. But in Alberta the total provincial income was made up of a fair share from manufactures, and from mining, and the returns from Alberta taxes on corporations and mines did not fall till later in the depression. Nevertheless, Alberta found it necessary to search out new revenues, and in 1922 both corporation and mine taxes were increased, as well as amusement taxes, and a new tax was imposed on gasoline (2 cents) and new revenues secured from liquor control. This represented some shift in

emphasis in the tax base, new weight being placed on taxes on industries, and on the spending of the people (amusements, liquor, gasoline). The shift to taxes on spending generally acts as a revenue stabilizer for governments in depression but only significantly so, if the economy is highly diversified, and if the households and firms are able to indulge in some "dissaving" in bad times, so that the spending of income falls less than the receiving of income. Taxes on spending are of rather less value as revenue stabilizers, to governments in agricultural communities, where there is little economic "balance", and where depression usually involves little "dissaving", (unless in the sense of failure to maintain capital), but rather tends to emphasize the burdensome nature of the private and public debts incurred in the previous boom.

In these conditions the Alberta government made considerable contractions in the expenditures between 1921 and 1924. The expenditure, both on capital and on ordinary account, had reached a high point in 1921, and it was therefrom contracted on both sides. In 1921, on capital account $9.0 million were spent on public works, $2.5 million on loans and investments, $4.7 million on railways, $5.7 million on telephones, and these, combined with the funds required on current account for a deficit of over $2.8 million, necessitated an increase in debt of over $25 million. The capital expenditure on utilities was reduced by one-third in 1922, and again in 1923, and the expenditure on public works was also curtailed, especially as between 1922 and 1923. This curtailment in capital expenditure on railroads, and on public works (especially bridges and highways), must have contributed to the contraction in the construction industry in Alberta during this period, as would also the fall in public works' maintenance charges on ordinary account. Nevertheless, the issues of new Alberta bonds kept high in 1922 and 1923, while the total for the provinces as a whole was declining rapidly

and the costs of Alberta's bonds began to increase their "spread" above the general average, while Saskatchewan kept below the general average.

On ordinary expenditures reductions were also made. But the debt charges increased rapidly. The expenditure on health also increased slightly, while all other expenditures suffered cuts, especially those on public works, and on costs of government; even education was curtailed slightly. But despite these changes in expenditures and in revenues, deficits continued until the trade recovery after 1924.

During this period certain changes had occurred in the international wheat situation. After the War increase in acreage and in mechanization, and with the good yields after 1922, Canada had become the leading wheat exporter, and was thereafter prone to the vulnerability of being important. The agricultural revolution had just begun in Europe after the war losses, and European acreage was only beginning to recover to pre-war levels, but the effects of this were hidden by the short world crop in 1924, and by the gradual revival in world trade, that increased world consumption. Although the per capita utilization never reached its pre-war levels, and although world production kept increasing, the general revival in trade permitted good "wheat" years from 1924 to 1927. In Canada, the effect was to increase wheat specialization still further, tractor sales mounted steadily, and mechanization affected also farm transport (and rendered much of the lately established railway mileage uneconomic, it being no longer necessary to have a railway at least within 20 miles of every farm). In Alberta the good "wheat" years reflected themselves in the manufacturing industries, and the total net value of production rose from 100 in 1921 to 245 in 1927, a rate much beyond that of the other Prairie Provinces. Under these conditions, the few adjustments that had been made in the revenue system in the 1921-3 depression were able to

reduce the current deficits. But there was no surplus until 1928.

The revenue from the real property taxes declined from 1925 to 1929.(2) The tax on lands under grazing lease was reduced in 1926, the wild lands tax had been reduced in 1922, and the unearned increment tax in 1921; and the assessment for supplementary revenue tax in 1926. Of the group of real property taxes only one, the unearned increment tax, increased its yield under the boom conditions from 1925 onwards, and the yield of the group fell by 33% so that while these taxes had formed 21% of the revenue in 1925, in 1929 they formed only 11%. Under the stimulus of the boom conditions, the yield from the taxes on spending increased rapidly, especially the returns from the gasoline tax(3) and from motor licences, with some increase also in liquor profits. The same impetus that was raising private incomes tended to raise the succession duty yield. The only tax charges made in the period were an increase in gasoline taxes from 2 to 3 cents in 1927, (in order to meet part of the expense for the new demand for highways), and a 5% tax on bets made under the pari-mutuel system. These increases were made in face of requests for tax reductions, and in all the budget speeches from 1925 to 1928, the government reminded the citizens that Alberta's taxation, in relation to its net production, was the lowest of all western provinces.

During the boom period up to 1928, the revenues were fairly buoyant, but the expenditure growth was such that a current surplus did not arise until 1928. In the early years of the boom, the capital expenditures had been kept constant, but as the boom advanced so did the volume of

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(2) From $2.3 million to $1.5 million.

(3) The gasoline tax yield rose from $0.3 million in 1925 to $1.8 million in 1929 and motor licence fees from $1.0 million to $2.0 million. Liquor profits increased from $1.6 million to $2.6 million.

government investment. In the early phase of the boom, the deficits on the public utilities were tending to diminish, the private indebtedness of farmers was declining rapidly, and all these conditions suggested a resumption of the economic expansion that the War had delayed. In these conditions, the demand on the government for new services (especially on highways) was insistent, and the buoyancy of revenues encouraged it. In the budget speeches, however, the government revealed some unwillingness to add to borrowing. The growth of revenues, expenditures, and capital works during these years may be indicated as follows:-

	1925	1926	1927*	1928	1929
		(millions of dollars)			
Revenue	10.7	11.1	14.6	14.1	14.5
Expenditure	11.4	11.9	15.5	13.1	14.4
Deficit (-) or Surplus (+)	- 0.7	- 0.8	- 0.9	+1.0	+0.1
Capital Expenditure	2.1	2.7	3.8	3.8	4.8
Over-all Deficit	2.8	3.5	4.7	2.8	4.7

*Fifteen month period.

This table indicates the growth of revenue in the boom years, the considerable growth in expenditures that prevented any surplus emerging until the peak year of the boom, and the tendency for capital expenditures to increase as the boom advanced. The capital expenditures expanded despite the frequently expressed unwillingness to add to borrowing. Before 1928, it appeared that if the railways could be sold to the Canadian National, and the Canadian Pacific Railways, and if the natural resources were given to the province, these changes, combined with the expanding revenues, would provide the means for the "legitimate development of the province in other directions". A further expansion of frontiers seemed desirable. And the statement made by Dr. Charles Saunders, that Canada had reached its maximum of specialization in wheat, the government thought applicable to Canada as a whole, but definitely not to the

Peace River Country. (Budget Speech 1929).

Between 1925 and 1929, ordinary expenditures rose by 27%. The net debt charge was the major item, and it rose by less than the total, accounting for 39% of expenditure in 1925 and 32% in 1929. The main increases were in public welfare and in highways, and these reflected the trend in all provinces. In public welfare, old age pensions began only in 1929, so that the main services that expanded were in public health (control of diseases, travelling clinics), in mental and tuberculosis institutions, hospital grants, and mothers' allowances. In highways, the work on main roads increased greatly, and grants to municipalities doubled. Expenditure on education also increased, especially the school grants. The main increases were as follows:

	1925	1929	Increase
	(Thousands of $)		
Net Debt charges	4,484	4,639	155
Public Welfare	1,544	2,526	982
Education	2,088	2,708	620
Highways	235	1,187	952
All Others	3,005	3,329	324
Total	11,356	14,389	3,033

Throughout the boom period to 1928, the investments in railways, telephones, etc. continued to be burdensome, but the increase in outstanding debt proceeded and for the boom years (1925 to 1928 inclusive), exceeded the debt increase in any other province, except Ontario. The increase was due partly to the deficits of 1925-7 and to the additional investment in public works, particularly highways and in utilities. The boom period it is true, was tending to increase the potentialities of certain investments and the deficits in some of the subsidiary enterprises of the government were declining. In telephones, the number of rural subscribers increased and this reduced the unprofitability of this part of the service,

which had always proved a drag on the exchange and toll systems. In railways, the expansion of the Peace River district suggested new possibilities, and railway traffic on that sector of the system reflected the changed conditions. Even the irrigation undertaking appeared to have some beneficial results in the encouragement of the sugar beet industry. Despite the boom conditions, however, the debt burden already exceeded that of any other province. As a percentage of expenditures, Alberta's annual net debt charges, less interest received, consistently exceeded 37% in the boom years as against less than 20% in the provinces as a whole.

Some relief to this position was forthcoming in 1929 when the government disposed of its railway lines to the Canadian Pacific and the Canadian National Railways. The net capital loss on realization was $11.4 million, but the receipt of an instalment on the purchase price in 1928 ($1.5 million) and in 1929 ($6.1 million) and the transfer of bonds ($0.3 million in 1928, and $9.4 million in 1929) to the Canadian Pacific and Canadian National Railways, allowed a reduction on the outstanding debt in 1929.[4] The debt position may be shown as follows for 1927 and 1929.

		1927	$ million	1929
Railways		37.3		
Telephones		21.0		21.9
Public Works		44.3		53.4
Other Advances, etc.		10.4		10.3
Capital Losses		.4		12.1
Deficits		4.7		2.9
Active Assets		14.6		29.8
		132.7		130.4
Less Sinking Fund Reserve	1.6		2.6	
Capital Surplus	.8	2.4	.9	3.5
Outstanding Debt		130.3		126.9

(4) Another reduction in outstanding debt, smaller this time, was made possible in 1933, when the second instalment ($5 million) of the railway purchase price was paid to Alberta.

The capital losses rose by the amount of the loss on railway realization.

Apart from the railway transaction, the main changes in the balance sheet in the boom years are shown by the increases in active assets and in public works. Active assets rose by $10.6 million as a result of the balance due on the sale of the railway. Public works expanded as a result of highway, public building and irrigation investment.

The history of Alberta's financial position in the post-war period turned on the growing significance of the debt burden. Even in the boom years, the debt charges (less interest received) never absorbed less than 37% of the net expenditure. Even in 1929 with high revenues and with some debt reduction, 32% of the net expenditures went to debt charges. And the advance of the boom seemed to reduce the "unwillingness" to add to debts. There had been some tax changes in the period, with a shift in emphasis from taxes on land to taxes on spending, and the latter (including liquor profits) became quite productive in the boom years. But their level was just sufficient to cover the growing current expenditures, and as the boom progressed, the demand for new current and capital expenditures seemed to indicate that a broader revenue basis would be desirable even if the boom were to continue. The great significance of the debt burden and the expansion of social and other services that were also difficult to check, were creating in the budget a large sector of inflexible expenditures. In such conditions Alberta required a broader and if possible a more elastic revenue system. And the history of the War and the post-war period was indicating that the more a provincial government has relied on extensive capital borrowings to expedite development, especially by the undertaking of risky ventures, the greater is the difficulty of resorting to this medium again.

The decline in agricultural income between 1928 and 1929 affected some of the revenue items in the latter year, the fall in licences and fees, in liquor profits, and in real property taxes reflecting the first effects of the changed agricultural situation. Manufactures, mining and construction trades did not contract until the following year, and their more prosperous conditon helped to hold up revenues as a whole. But as the depression became general, revenues as a whole suffered, and by 1931 were 15% below the 1930 level. This fall was relatively smaller than that suffered by Saskatchewan. Nevertheless, the whole revenue revealed its sensitiveness to economic change. The fall in land taxes reflected the changed agricultural situation; the fall in gasoline taxes and in passenger automobile licences reflected the lowered spending power, as did also the fall in liquor sales from $6.5 million in 1928 to $3.6 million in 1932, and to $2.4 million in 1933, and the growth of the operating deficit in the telephones. The revenue changes between 1929 and 1931 were as follows:

	1929	1931	Increase	Decrease
		(Thousands of $)		
Public Domain	166	988	822	
Subsidy	1,577	1,743	166	
Refunds & Sales	429	511	82	
Taxes	5,518	3,951		1,567
Liquor Control	2,586	1,424		1,162
Licences	3,245	2,448		797
Fines & Other	968	633		335
Total	14,489	11,699		2,790

In 1932, corporation and gasoline taxes were raised and an income tax imposed, and this helped to raise the 1932 revenues, but in 1933 the gain was barely held and further revenue efforts were necessary, only the returns from the gasoline tax, from motor licences, and from the public domain showing any buoyancy in 1933.

The revenue system was therefore in process of change, under the impact of the depression. Increased returns were being received from the public domain, as a result of the grant of the natural resources in 1930. The royalties and rentals from coal, gas, and timber, which were to increase after 1933, represented a shift in the revenue system that was independent of the depression. But as the depression persisted, the changes in corporation taxes, and the introduction of the income tax, represented attempts to widen the tax base to secure revenue, and also to widen it in a way that would permit the province to get some more stable revenues, particularly from corporations that operated nationally. In the same way, the later resort to a retail sales tax may be described as a search for a tax on spending sufficiently broad as to give stability to the revenue. On special commodities of heavy demand, old taxes were increased, e.g. gasoline in 1933, and 1935 and in 1936 the province took over the distribution of beer. Although the retail sales tax was suspended later, there is evidence in the whole period of attempts to widen the revenue basis from specific taxes on spending, on land, corporations, etc., to more general taxes on spending.

The revenue changes, and the economic recovery after 1934 yielded some recovery of revenue. The significant increases were as follows:-

	1933	1936	Increase
	(Thousands of $)		
Taxes	4,909	7,393	2,484
Liquor Control	1,251	2,400	1,149
Domain	972	1,541	569
Total Revenue	12,609	17,048	4,439

Some of the revenue increases were partly offset by a decrease in the revenue from licences (particularly motor vehicles). The increase in tax revenue came mainly from the short-lived retail sales tax (accounting for 38% of the increase), the gasoline tax (31%), the real property and corporation taxes

(each 11%), the income tax(4%) and the remainder from the succession duties and amusement taxes.

On the expenditure side, some reductions were made, especially in 1932, but by 1935 expenditures as a whole had increased again. The net debt charges remained high, and by 1933 absorbed over 37% of the expenditures: for this reason alone, expenditure reductions were rendered difficult. The costs of government were reduced by salary cuts in 1932, but this method of securing economy in expenditure was of limited use. Public welfare was reduced slightly, but the main reductions between 1930 and 1933 were in education and highways. In so far as these are of the nature of "capital" or development expenditures, the depression was causing the province to reverse its former policy of investing in the future, and by the cuts in expenditures on its physical and human resources, the depression revealed that the province had to concentrate on immediate, rather than on long-term, needs. To some extent, however, these expenditure contractions on highways were made by the reduction of grants to municipalities. By 1936, there was a considerable increase in highway expenditure, a trend that is likely to continue for some time into the future, given available revenues.

The significant expenditure changes between 1931 and 1935 were as follows:

	1931	1933	1935	Change 1931-3	Change 1933-5
		(Thousands	of $)		
Net Debt Charges	6,377	6,027	6,112	- 350	+ 85
Welfare (excluding relief)	2,884	2,410	2,695	- 474	+ 285
Education	2,661	2,438	2,469	- 223	+ 31
Highways	1,620	781	726	- 839	- 55
Government (including Justice and Legislation)	2,790	2,305	2,585	- 485	+ 280
Total Expenditure	18,846	16,429	17,151	-2,417	+ 722

By 1935, total current expenditure had recovered to 91% of its 1931 level. The only services that had increased were relief, legislation and general government.

Despite the cutting of debt charges in 1936, the total expenditure in 1936 was still slightly in excess of the 1930 level. The attempt to meet relief requirements from the budget (by an

increase under the heading of welfare) rather than from borrowing, has, despite the debt default, considerably curtailed the funds available for education, agriculture, and highways, (the total of which in 1936 was 25% below the 1930 level), as well as the funds available for the services usually covered by public welfare, like public health, child welfare, etc. The inclusion of over $2.6 million of unemployment relief in the ordinary budget in 1936 went far to absorb the revenues that would have gone to meet the normal debt charges.

The decision to reduce the interest rates, reduced the net debt charges from $6.1 million in 1935 to $3.8 million in 1936.

Despite the adjustments in revenues and expenditures, deficits on current account persisted, reaching a peak in 1931, and remaining stable on a somewhat lower level from 1932 to 1935. The capital requirements were high in 1930 as a result of the expansion of public works and telephones in the later phase of the boom, and as a result of new depression expenditures for relief work on highways, and for additional advances to the Hail Insurance Board, the Co-operative Credit Societies, etc. In 1931, the current deficit reached its peak of over $7 million, so that although the capital requirements were smaller than in the previous year, the over-all deficit continued to rise. The public works and telephones were considerably curtailed, but to some extent the reductions were offset by increased capital expenditures on relief, and by a special loan of $5.6 million to the Alberta Wheat Pool. In all the total funds required were still at the 1930 level, and since revenues were down in 1931, additional borrowings had to be made, so that the increase in outstanding debt was high in 1931.

	1930	1931	1932	1933	1934	1935	1936
			(Millions of $)				
Revenue	13.8	11.7	12.9	12.6	13.9	14.3	17.0
Expenditure	16.3	18.8	16.6	16.4	16.7	17.1	16.6
Deficit (-) or Surplus (+)	- 2.5	-7.1	-3.7	-3.8	-2.8	-2.8	+ .4
Capital Expenditure	8.3	4.7	2.5	.9	2.7	4.4	1.5
Over-all Deficit	10.8	11.8	6.2	4.7	5.5	7.2	1.1
Increase in outstanding debt	11.4	16.3	4.7	-1.0	6.6	6.9	-1.4

The cuts in capital expenditure after 1930 continued up to 1933, and the current deficit after 1932 was stable. With the small over-all deficit in 1933, and with the receipt of $5 million from the instalment of the railway purchase price, a small reduction in outstanding debt was made possible. The increase in debt was resumed in 1934 and seemed likely to persist, until the cutting of interest charges in 1936. By thus leaving $2.7 million of interest unpaid, Alberta was able to effect a small debt reduction in that year. The rise in capital expenditure for the low level in 1933 was due partly to a slight resumption in public works, partly to the distribution of seed grain (1935), and other expenditures connected with the irrigation districts, loans to improvement districts, and expenses on the movement of settlers.

In the financing of its debt growth after 1930, the partial reliance on direct issues that characterized the depression years (up to 1932) gave way to treasury bill financing, placed with the Dominion government, the banks having held few bills since 1931. The steady withdrawal of savings certificates on demand from 1930 onwards made the financial position even more difficult, and although the province managed after 1932 to transfer part of these savings to a term basis, the withdrawals of these also from 1935 onwards has increased the government's need for funds. The reduction in liquor revenues, and the losses on the Alberta

telephones, were so large as to demand changes in policy. The reduction in liquor revenues induced the province in 1936 to take over the distribution of beer, which increased the revenue by half a million dollars. With respect to telephones, the rural losses became much too heavy for the system, and after a special investigation in 1934 the province cut its losses on the rural lines, either by selling them at nominal prices to mutual companies, or by scrapping them.

By 1935 the net debt charges accounted for 36% of the expenditure as against 22% for the provinces as a whole. (The arbitrary reduction of interest paid on Alberta bonds in 1936 lowered the proportion of expenditure that went to net debt payments to 23%, almost the level that held for the provinces as a whole.) By 1935, the budget-balancing efforts had not been particularly successful, the current deficit having remained almost unchanged from 1932 onwards. The revenue system had been broadened, but new efforts appeared to be necessary, although the burden of private indebtedness within the province seriously limited the taxable capacity. Expenditures on almost all items had been reduced, but debt and relief stood out as the two inflexible factors, while many services formerly considered essential (highway, education, and welfare) had been seriously curtailed. Although the debt growth from 1930-5 had been at a very much lower rate than in Saskatchewan, this debt growth in Alberta was superimposed on a debt structure that was already very heavy, and with its great need for funds in 1930 and 1931, the costs of borrowing had risen steeply against the province. This burden, combined with the fact that most of the debt was held outside Alberta, was rendered especially heavy with the fall in income, and the turning against Alberta of the terms of exchange between it and the debt-holding areas at home and abroad.

The balance sheet for 1932 and 1935 indicates the steady worsening of the financial position.

		1932	(Millions of $)	1935
Active Assets		32.7		27.6
Telephones		24.5		16.1
Public Works		66.8		72.3
Other Advances		16.4		24.5
Deficits		11.9		17.5
Capital Losses		13.1		23.3
		165.4		181.3
Less Sinking Fund Reserve	5.3		7.5	
Capital Surplus	.8		1.2	
Deferred Revenue	-	6.1	.8	9.5
Total Outstanding Debt		159.3		171.8

The active assets were reduced by the payment of the railway instalment in 1933. In 1933, 1934 and 1935 a total of $8.9 million were written off the telephone system. The deficits had grown, and so had the non-interest bearing advances and the capital losses.

The decision to default on the payment of full interest on the bonds altered the financial picture considerably, by cutting the debt charges in half. The transference of relief to income account largely compensated this decrease in debt charges in 1936, as already indicated. At the same time, considerable revenue increases, especially from the new sales tax, (that has since been removed), permitted an approximate current balance in 1936. There was also a great reduction below the 1935 level in the capital expenditures on public works, and on loans and advances so that in 1936 only $1.1 million were required for current and capital accounts, (i.e. over-all deficit).

By 1937 the province was already making tax efforts that are fairly comparable to those of Saskatchewan, and if the short-lived sales tax be considered, probably comparable with those of Manitoba. But the contraction of borrowing, and the meeting of relief from income account, has reduced the amounts available for capital expenditures, as well as for development and maintenance services within the ordinary budget, (e.g. highways, education,etc.). In other words, the change of emphasis in

the government activities (as reflected in expenditures) is now directed very largely at income transfer within the community rather than at development. If relief charges become smaller, this position will improve, by increasing the portion of revenues available for development expenditure. But unless borrowing can be resorted to, capital expenditures for developmental projects will be limited to the buoyancy of the revenues.

<u>Summary</u>

(1) The present financial position of Alberta has to be considered in the light of the pre-war and War periods, during which the province engaged in increasingly extensive capital commitments. By 1921, the debt charges, (less interest received)) absorbed about one-quarter of the net revenue, a proportion considerably above that for the provinces as a whole (16%).

(2) The investments had been largely based on optimistic expectations with respect to the future economic potentialities of the region, and since the region was new, the danger of error in the investment was not inconsiderable. The post-war period saw some further pursuit of this investment policy, along with the expansion of services that were common to all provinces, particularly the social services, and highway construction. During the post-war period, there was some little broadening of the revenue basis, but in view of the fixity and the size of the debt charge, the revenue system barely managed to cover expenditures until the peak of the boom (1928).

(3) The depression following 1929 revealed the rigidity of the expenditure system, and the preponderating influence of the debt position. As in other provinces, the depression also tended to raise certain welfare expenditures. In view of the fall in regional income, revenues could not prove buoyant, and since debt and welfare absorbed so large a share

of the expenditures, cuts had to be made in other directions. By 1936, the revenue efforts were comparable to those in the other Prairie Provinces. Since interest was reduced in that year, and since there was some economic revival and some expansion of revenues, relief expenditures were met from the ordinary budget. Capital works remained low however, and developmental activities in the budget were mostly below the previous boom levels.

Financial Position of British Columbia.

While British Columbia resembles the Maritimes in being on the circumference of a protected area in which the forces that make for centralization are strong, and in being dependent for its regional income very largely on external trade, yet its public finance system has been in the main determined by factors not found in the Maritimes. Of these factors, the geographical one is, and has been, the most important determinant of British Columbia's financial history. The presence of gold provided the initial force towards settlement, and the abundant timber, fisheries, and diversity of minerals, added impetus to the initial movement of population to the west coast. The geography, however, dictated also the direction of the settlement within the colony itself, and made the region as a whole difficult to traverse and probably expensive to administer, as population spread fanlike from Vancouver. The historical development of British Columbia has also contributed towards creating a public finance system that differed from that of the Maritimes. The comparatively recent settlement, the impact of the almost revolutionary opening of the west in the early 20th Century, achieved a boom and a rate of economic progress that the Maritimes never encountered. The effect of this growth, and the sudden penetration of the large pioneer fringe of British Columbia, led to costs of frontier expansion in new roads and railways. It led also to costs of administration in the wide areas of unorganized territory, and these costs of development and administration may have been high per unit of population because of the geographical nature of the country.

From union up to 1905, British Columbia encountered a series of budgetary deficits that were unique in size in Canadian history, followed from 1905 to 1912 by a series of surpluses that were equally unusual in amount, and these in

turn were followed by another series of deficits to 1918 that were also unusually large. Since then, a more normal relationship has existed between the rate of expenditure and revenue increases. But this history of deficits is worthy of comment. As with all governments, part of the deficit was attributable to the difficulty of forecasting expenditures and revenues: and in British Columbia, especially in the pre-war boom, and the early war depression, the difficulty of correct forecasting was increased by reason of the nature of the economic change that was taking place. But the deficit financing in British Columbia at this time was much more a matter of fiscal policy than financial miscalculation. While other provinces elected to meet their capital works by the orthodox method of borrowing, British Columbia chose to meet them largely from current account. The government estimated for deficits, and in the period of expansion, there was much justification for such fiscal policy in British Columbia. So rapid was the economic development that only very approximate calculations of expenditure needs could be made. And the size of revenues was also difficult to gauge. Furthermore, since so large a part of the revenue in the pre-war period came from the utilization of resources, particularly lumber, revenues did largely represent capital utilization, and the meeting of capital works from such revenues had good economic justification. Accordingly, by 1921, when the reported accumulated current deficit reached $29.5 million, which was high as compared with other provinces, the real deficit was approximately $4 million, after allowing for the $10.2 million "deficit" that had been spent on highways and communication equipment, the $10.9 million that had been spent on public buildings, and the change that had been made in current assets, etc. Similarly the reported accumulated

current deficit of $53.4 million in 1936 (i.e. fiscal year ending March 31, 1937) could be adjusted downwards to $26.3 million by allowing for the capital expenditures that have been charged to current account, (and for some of the capital receipts that have been credited to current account).(1)

In British Columbia it was in the pre-war period that the practice of meeting capital works out of ordinary account was general. The transition from the depression at the end of the 19th Century to the boom in the early 20th had an unusually marked effect on the buoyancy of British Columbia's revenues. The unfavourable condition at the end of the century showed itself in the fact that five governments held office in the five years following 1898. It showed itself also in the case made by the Province at the inter-provincial conferences in 1902 and 1906. Revenues had not been buoyant in the 90's, unintentional deficits emerged, as already indicated, and the cost of administering the Province, the cost of providing its roads, schools, buildings, and hospitals, tended to be fairly high because of the physical configuration of the country and the spreading of settlement. In 1902 and in 1906, the Province emphasized this special condition before the inter-provincial conference. The effect of the tariff policy on the west was also raised, and the

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(1) While these accountants' adjustments (Appendix K, Schedule 1A) concern mainly physical capital expenditures that have been charged to current account, and include also allowance for certain capital receipts that were credited to current account, no adjustment can be made to indicate how far certain current revenues (e.g. from lumber or other natural resources) involved also an element of capital utilization. From an economic point of view, revenues that involve depletion of resources are also an instance of capital receipts that are being credited to current account.

necessity of buying from the east at sheltered prices, and selling in the world market at exposed prices was indicated. In addition, British Columbia in 1902 raised an issue that has since been emphasized more in other confederations than in this: the fact that when the Province secured immigrants (or imports), it had to contribute to Dominion customs revenues; in the case of immigrants it contributed indirectly by having to maintain immigrants, whose purchases raised Dominion customs revenues: in the case of imports, which were often purchased by borrowing, the Province had to pay an enhanced price which went to the Dominion revenues. In 1902 British Columbia raised the point with particular reference to immigrants.

The advance of the boom however tended to make the geographical position an asset rather than a liability. The presence of timber, the beginning of shipbuilding, the construction of the Panama Canal, made the geographical factor an important contributor to the optimism of the period. The possibilities of mineral development seemed great: the opening of the Prairie Provinces provided both a construction and a railway boom that increased the immediate demand for British Columbia's resources, and indicated new long term possibilities. The buoyancy of conditions began to be marked by 1907. So far as they affected government revenues, land sales and timber royalties formed the significant increases, but under all heads, increases were so great that it was difficult for expenditure to keep abreast of the expanding revenues. Some tax reductions were made in personal taxes and bridge tolls, some loans paid off (e.g. the 1903 loan of $1 million), but despite this, a considerable surplus was left in the bank, amounting to $6 million in 1908 and to $9 million in 1911. The total funded debt, after deduction of sinking funds, amounted to $9.2 million in 1909. In the

Budget Speech, the treasurer decided to keep the surplus for a "rainy day". In these buoyant conditions, considerable increases in expenditure were made, and although the government budgeted for deficits, so expansive were the revenues that deficits did not emerge until 1913.

The large expenditure increases began in 1909. Expenditure, as reported by the Province, had amounted to $3.6 million in 1908, and by 1913 it reached $15.8 million. Out of this current expenditure, however, a large amount went on capital works. From the accounts it is clear that $1.1 million were spent on general government buildings, $0.5 million in gaols, $0.3 million on mental and other institutions, $0.2 million on schools and $0.2 million on debt amortization. In all, at least $2.3 million of the $15.8 million went to capital works. But the amount spent on capital works in that year was certainly more than that which can be calculated from the public accounts. On highways $3.6 million were spent on maintenance, and on bridges $1.0 million; the amount that went on construction is not indicated, but it probably was significant. Neglecting highways, however, it is clear that the $15.8 million expenditure involved capital expenditures to the extent of $2.3 million, and debt amortization of $0.2 million. In addition, interest revenue, which is a deduction from debt charges, amounted to $0.2 million. Consequently current expenditures were $13.3 million. Since it is impossible to separate out the capital works being done on highways, this item appears to dominate the current expenditure system in 1913, accounting for 40% of the current expenditures in that year. The second expenditure item was education, amounting to 15% of the total, then government 13%, domain 12%, justice 8%, welfare 7% and net debt only 1.1%. The total outstanding debt was $25.6 million, excluding $25 million contingent obligations in respect of guaranteed bonds of the Canadian Northern Pacific Railway.

In this period, the developmental expenditures were considerable, and they were being financed very largely by public

domain revenues, by timber revenues and land sales. In 1913 they yielded 37% of the revenues, or $3.7 million. In the previous year, however, at the peak of the boom, their yield had been $4.9 million. By 1913, therefore, the first year which the public accounts inquiry of this Commission covers, the full importance of the timber and land revenues during the boom, is not indicated. It had been the constant rise in these revenues that had permitted the new developmental expenditures, and that had built up cash reserves. Their buoyancy also had helped to create long term expectations that were optimistic: the most optimistic expectations of 1906, with respect to both economic expansion and domain revenues, had been far exceeded by 1910. The law of acceleration was such that expectations had no base from which to project themselves. In such conditions, the cost of widening the frontier fringe seemed unimportant: revenues existed and surplus amounted, and new frontiers seemed likely to add to this progress. New commitments on roads and buildings seemed necessary, and since railways were also a necessary condition for settlement, especially in the northern hinterland and towards the Peace River country, the government undertook obligations with respect to the Canadian Northern Pacific Railway, and the Pacific Great Eastern.

The rate, and the nature, of the expansion of government undertakings at this time were typical of a great boom: the growth of optimism and the cumulative additions to construction that come when a certain project seems justifiable, and when the very process of constructing that work so adds to income (and consumption) that additions to the project, and even new projects, seem called for: the not inconsiderable amount of haste, strain and overwork that accompany booms, and that make rational decisions more difficult, and careful supervision more perplexing: the apparent unimportance of the question of cost in face of the financial smoothness.

In British Columbia, when the boom broke, the costs of social services and of debt were unimportant. But

the surplus which the treasurer had been saving for a rainy day had been spent in part, it having been considered wise to use the surplus for development purposes "rather than to wait until this want should constitute a grievance". Furthermore, following on the recommendations of a commission on taxation, it was indicated in 1913 that the tax system would be altered, that the poll tax would be abolished, and that "improvements" would be exempted from taxation.

The tax reduction coincided with the first real curtailment of economic expansion, the revenue falling from $12.4 million to $10.2 million between 1912 and 1913. The land boom was breaking, and land sales fell by over one million dollars, immigration was slacking off, the Chinese Restriction Act revenue alone showing a fall of over half a million dollars, and economic conditions generally were revealing the effects of the ending of the world boom, coal royalties being down and lumber returns contracting. At the same time, the provincial government felt the loss of interest that had dwindled as a result of spending its "rainy day", surplus. The deficit on ordinary account was over $3 million during the fiscal year ending in March, 1914; the over-all deficit almost $20 million.(2) The sudden change in conditions in 1913 was unexpected, and the general financial stringency occurred just at the point when British Columbia had entered the maximum of commitments. There were over 3,000 miles of railways under construction, as well as other works on roads and buildings. The following table shows the funds required, and how they

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(2)

		1913 $000
Current Revenue		10,154
Current Expenditures		13,310
	Current Deficit	3,156
Capital Expenditure		16,511
	Over-all Deficit	19,667

The decrease in the cash balance was over $4 million in that year, and the addition to debt $15.9 million.

were provided in 1913.

	$000		
Current Expenditure	13,310	Current Revenue	10,154
Capital Expenditure		Borrowings	15,919
Buildings	2,115	Decrease in	
Railways	14,235	cash in bank	4,110
Other	161		
Other Expenditures	362		
Total required	30,183	Total provided	30,183

The large government capital undertakings begun in the boom period were not all amenable to rapid curtailment: railroads, roads, and buildings, in process of construction, had to be completed, so that these expenditures could be tapered off only gradually. Accordingly, public works (including highways and buildings) were gradually reduced from $7.4 million in 1913 to $2.2 million by 1918, and total expenditures (i.e. current plus capital expenditures on buildings, etc.) from $15.7 million in 1913 to $12.1 million in 1918, the fall being almost entirely due to the contraction in public works. The railroad expenditures continued, however, and exceeded the Province's estimated costs, especially on the Pacific Great Eastern Railway. The road had been conceived in the later boom days, and had been intended to tap the full resources of the Canadian North West. The government in 1912 undertook to assist a company established for the construction, by payment of subsidy and guarantee of the company's bonds. The government was lax in supervising the paying out of the trust fund, and the company quickly exhausted the fund, and suspended work with only a short distance constructed. The government had to take over the line in 1917, cover the defaulted bonds, and proceed with the construction. This ceased in 1921 with the Quesnel-St. George section incomplete, and the first train ran from Squamish to Quesnel in that year. The government found it necessary also to try to increase the utility of the line by adding further equipment, (wharves, cattle corrals, light and power systems, housing at Squamish, etc.).

The result of the change in financial fortunes in 1913-14 was to drive British Columbia into the capital market and the government resumed borrowing in 1914, after a ten years' lapse. It had to borrow heavily in 1914, and again during the War and post-war years. While outstanding debt in 1913 had been $25.6 million,(3) the figure in 1921 was $80.3 million. There was therefore a significant change in the public finance system in British Columbia during this interval, a change that reflected itself, not only in the growth of the outstanding debt, but in the structure of both the expenditure and revenue systems.

The effect of the breaking of the boom was to create a marked contraction in revenues. They fell by 50% between the last boom year 1912, and the depression year 1915. The decline in revenue was about $6 million, and the major contributors to this decline were land sales, and timber licences. They fell by $3.3 million in this period. It became clear, as the depression advanced, that the buoyant revenues had been associated with special boom conditions, and with the sale of the domain of the Province. The need for a wider revenue basis was obvious. Land sales have never again reached the 1912 level, although in the post-war boom (1919-20), timber revenues again reached the 1912 levels. In subsequent booms, they also got back to this peak. But as the Province's commitments expanded in the early years of the War, and as domain revenues contracted, the search for a wider revenue basis began. In 1917, as large deficits continued despite the cuts in expenditure, particularly on public works, a change was made in the tax system, and new emphasis was given to the income tax, land tax, and personal property tax. The latter was repealed later, but the income tax and land tax, particularly the former, achieved new significance in the tax system. They were made to yield about 60% of the tax revenues, a proportion which they still hold, despite later tax changes. In 1917 also, other tax changes were made:the poll tax that had been

(3)Excluding $25 million contingent liability in respect of guarantees of Canadian Northern Pacific Railway bonds,subsequently assumed by the Canadian National Railway Company.

repealed was re-instituted, taxes were laid on amusements and liquor profits were tapped. These tax changes happened to coincide with the war boom (1917), and tax revenues proved buoyant till 1921; indeed revenues as a whole passed their 1912 peak by 1919, and the rate of increase was again comparable to that of the pre-war period. Revenues increased from $6.9 million in the fiscal year ending March 31, 1917, to $15.2 million in the fiscal year ending March 31, 1920; about half of this increase came from income tax, and from the natural resources revenues, and the remainder from motor licences, amusements, succession duties, school tax and fees.

As revenues expanded after 1917, so also did expenditures. Debt charges, however, had increased steadily from 1913 to 1917 as a result of the deficit financing, and although they steadied in 1918, they resumed an upward trend again because of new government commitments undertaken at the close of the War.[4] Between 1917 and 1920, expenditures as a whole were doubled, the main increases being in public works (roads and general buildings), education, and debt, with smaller additions to hospitals, justice, natural resources, and pensions.

It has been indicated that the outstanding debt rose rapidly from 1913 onwards. Excluding the guarantee of Canadian Northern Pacific Railway bonds, it increased by almost $55 million between 1913 and 1921. The increase in outstanding debt in this period (1913-21) was accounted for in this way:

		$000,000
Increase in		
Current Assets		12.5
P.G.E. Advances		20.5
Public Works		22.2
Other Loans and Advances		9.9
		65.1
Decrease in current deficit	5.3	
Increase in Sinking Fund Reserve	5.7	
	11.0	
Decrease in capital surplus	.6	
	10.4	10.4
Increase in outstanding debt		54.7

(4) In 1913 interest on direct debt had accounted for less than 3% of expenditures, but by 1917 debt charges reached almost 30%.

The increase in debt was in large part attributable to the railway situation, which compelled the provincial implementing of the Pacific Great Eastern Railway guarantees from 1916 onwards, and to the rapid increase in many commitments towards the end of the War.

The railway advances between 1913 and 1921 amounted to over $23 million but over $3 million were met from current revenue. The public works investment in 1921 showed $13.4 million in highways, and an increase of $8.6 million in public buildings. The university investment expenditures were beginning in 1921. The increase in current assets reflected a series of commitments that really began towards the end of the War. The Better Housing loans began in 1919, and by 1921 (i.e. March 1922) reached $1.6 million. The Vancouver and District Joint Sewerage and Drainage Board investment by the government, amounted to $3.2 million in 1921, and assistance to municipalities was $0.9 million. The other factors adding to current assets between 1913 and 1921 were changes in the cash position, the amount of taxes receivable, etc.

The increase of $9.9 million in other loans and advances was attributable to several policies: the Land Settlement Board advances amounted to $3.6 million, the Soldiers' Land Act advances, begun in 1919, amounted to $2.4 million in 1921, the Dyking district advances to $1.4 million (of which $0.7 million had been written off), the conservation fund, begun in 1919, had absorbed $1.4 million by 1921, and the Agricultural Credit Commission $1 million.

The breaking of the post-war boom, and the emergence of depression in 1921 created again a financial position not unlike that of the period after 1913. Although the revenue system was broader in 1921, the commitments were greater, the volume of debt and welfare larger, and the financial position of the municipalities more precarious than before. The

municipalities, which included three-quarters of the population, but covered less than 1% of the area, had failed to recover from the over-expansion of the boom period. The local improvements and public utilities tended to exceed local needs, and this led to large debts, failure to meet sinking fund payments, and heavy arrears of taxation. In 1921-2 the provincial government gave aid to the municipalities to help with relief, education, and mothers' pensions, and shared with them the motor vehicle taxation and liquor licences. The grant from provincial revenues rose annually, and by 1928-9 amounted to $2.0 million: the advent of the depression after 1929, and the reduction of provincial revenues, then called for a change in the amount and method of grants.

The ordinary expenditures indicated the growth of certain provincial commitments between 1913 and 1921.

	1913	1921	Increase
	$000	$000	$000
Net Debt charges	151	3,198	3,047
Welfare	873	2,364	1,491
Education	1,968	3,358	1,390
Miscellaneous	173	1,245	1,072

These represented the outstanding increases in current expenses. The increase in "miscellaneous" arose from the new grants to municipalities. The education increase arose from an increase in school grants (mainly primary schools), from the new level of current expenses in the university, and from miscellaneous education expenses. On welfare the two main additional expenses were on provincial institutions and on the new service of mothers' allowances. Unemployment relief also added to this charge. In 1921 British Columbia's expenditure on welfare and education absorbed about the same proportion of total expenditure as in the provinces as a whole, but her net debt charges were higher. The fixity of debt charges and the tendency for welfare and education costs to rise, meant that a fair proportion of

the province's expenditure system was comparatively uncontrollable. The revenue system on the other hand, was liable to fluctuation because the source of the province's regional income was mainly from exports. The revenue structure was broader than in most provinces, since it was composed of many different tax and non-tax revenues, but the source of all the revenues was an income that depended primarily on export trade.

The width of the tax structure is indicated by the fact that the province employed (1921) taxes on both real and personal property, corporation taxes (including net income), income tax on persons, poll tax, succession duties, and a tax on entrance to places of amusement: that these taxes were important in content as well as in form is indicated by the fact that they yielded 42% of the revenues in 1921. The second important source of revenue was the public domain: the timber revenues were down in 1921, after their post-war peak, but in 1921 the domain yielded 24% of the revenue. The third source, and a more recent one was from liquor control, which gave 16% of total revenue. Licences were the next important item, yielding 10% of total revenue, half of the licence fees then coming from automobiles. These four sources yielded 91% of the revenue: federal subsidies, and other revenues were already of very minor importance in British Columbia's broad revenue scheme.

The breadth of the revenue system was such that it tended to catch the income that was available, and revenues held up well in the post-war depression. British Columbia did not suffer to quite the same extent as Canada as a whole in the 1921 depression, but some quick recovery in mining, manufactures, and construction, produced some balance in the economy, and established a rate of economic growth from 1922 on to 1929 that probably exceeded that of Canada as a whole. By 1922, although the provincial government suffered reduced returns from its timber licences, the recovery in the secondary industries

increased the yield on income tax, on personal property taxes and on motor licences, so that the revenues of the fiscal year ending in March, 1923, showed a considerable increase. This buoyancy prompted in 1923 a new policy of tax reductions that continued, with annual concessions to taxpayers, almost to 1929. The revenues did not fall, because as had been indicated, this period was one of considerable growth in wealth, but the effect of the tax reductions was to offset the increased buoyancy of yield, so that in effect tax revenues increased little in the four boom years from 1925 to 1928. Their yield increased only from $9.7 to $10.0 million, the increased yield in corporation taxes and the slight additional yield from gasoline, personal income tax and succession duties, being largely cancelled by reduced yields from personal and from real property taxes and from poll tax. Indeed in the boom years to March 1929, the only buoyancy that revenues showed was in liquor profits and automobile licences. Liquor profits increased by $883,000 and licences by $781,000, but the latter was offset by declines in other revenue items, revenues as a whole rising only by the added amount of the liquor returns. The tax changes which tended to prevent the rising regional income from causing a proportionate rise in revenues may be indicated as follows.

In 1924 the tax on farm lands was reduced from 1% to one-half of 1%, and so also was the tax on personal property. Motor licences were cut by 25%, and amendments were made to the Succession Duty Act, giving exemption to bequests. The amusement tax was cut from 10% to 7%. As against these reductions, a 3 cents per gallon tax was imposed on gasoline, and a tax on fuel oil, which was later declared ultra vires. It was withdrawn in 1926 but re-enacted in 1932. In 1925 and 1926 further reductions were made, this time in income tax rates, and increased

rebates were given to married persons, and for dependents. The personal property tax was again reduced, and later abolished. In 1927 a tax on gross income was substituted, graduating amounts payable according to trades, professions and business. Again amusement taxes were reduced now from 7% to 5%. A change in the Succession Duty Act increased exemption, made allowance for insurance, and tried to cope with the double-taxation question. The coal lands tax was reduced from 4% to 2%. As against these reductions, a new tax was laid on banks. Over all, however, the concessions granted in these years meant a considerable loss of revenue, despite the new taxes, and when expenditures began to get ahead of revenues in 1928, new revenue sources had to be sought.

There was a current deficit in 1928, and it happened to coincide with an extension of capital expenditures (mainly for highways, begun in 1927) and this led to a considerable over-all deficit in 1928. The following table indicates the position during these boom years.

	1925	1926	1927	1928 (i.e. March 1929)
		$000		
Revenue	21,204	21,884	22,832	23,116
Expenditure	19,069	20,058	21,195	23,933
Surplus	2,135	1,826	1,637	-817
Capital Expenditure	-472	2,708	4,297	5,249
Over-all Deficit	-2,607	882	2,660	6,066

It will be seen that there was a rise in both current and capital expenditures in these years. On current account the main increases were in welfare, education and net debt, these accounting for 76% of the increase. The remainder went mainly to highways and government. The increase in welfare expenditures arose from the introduction of old age pensions in 1927, and from the increased expenditures on institutions and hospitals. The increase in education came from the enlargement of school

grants, particularly for buildings, from new expenses on industrial education, and from increases in advances of rural school district taxes. The net debt charges rose as a result of the growth of debt from $94.9 million to $105.6 million. The growth of debt was due mainly to the extension of the investment in highways (from $20.7 million to $29.7 million), and also from new work on buildings (from a level of $12.5 million to $13.8 million in the assets).

The expansion of the over-all deficit in 1928 was met by a considerable increase in revenue in the following year. The increase came mainly from taxation, but liquor and automobiles continued to rise very much as they had done throughout the whole boom period. The 1929 increase in tax revenues came largely from the corporation taxes, principally the tax on gross income of miscellaneous companies. This increase in revenue allowed again a surplus on current account, but in 1929 the capital expenditures were larger than in 1928, so that the over-all deficit continued to grow. Capital works had been enlarged after 1927, and this investment reached its peak ($9.3 million) in 1930, after which it declined gradually to 1931, and then ceased until the period of economic recovery after 1934. As a result, the debt increases tended to become greater in the boom, reaching a peak in 1930, and then diminishing with the decline in private investment. The over-all deficit in British Columbia since 1930 was as follows:

	1930	1931	1932	1933 $000	1934	1935	1936
Current Deficit	2,175	4,701	4,552	3,067	1,849	988	104
Capital Expenditure	9,305	4,930	730	132	1,317	3,266	3,551
Over-all Deficit	11,480	9,631	5,282	3,199	3,166	4,254	3,655

In 1932 the capital works on highways ceased almost entirely. Since 1934 relief work on highways and in 1936 customary and capital works on highways, have increased the capital expenditures. The annual increase in debt, however, has

not resumed its boom levels.

The size of the current deficit during the period was affected by the relief expenditures. The contraction in world trade from 1930 to 1932 greatly affected British Columbia's export trade, but as a result of the later recovery in forestry, mining, and manufactures, British Columbia tended to suffer over the period from 1930-7 no more than Canada as a whole (i.e.not so much as those export areas that depended largely on single crops). The depression problem, as in most other provinces, was mainly a relief problem, and British Columbia had been involved in direct relief payments amounting to $24.2 million. Since 1931, the annual payments have been $1.9 million in 1931, $3.6 million in 1932, $3.6 million in 1933, $4.6 million in 1934, $5.1 million in 1935, and $4.4 million in 1936. In addition almost a quarter of a million has been spent on grants for municipal works, $5.4 million for relief work on highways, and $0.9 million for other relief work, most of it in 1935. Although almost all these relief payments were capitalized, only those spent on works are covered by assets. The direct relief (of which $21.7 million was capitalized) has been a consumptive expenditure and has been added to the welfare charges. As a result, welfare charges have tended to rise annually since 1930, the only check being in 1933, when hospital grants and mothers' allowances were lowered: The relief expenses, however, rose annually to 1935. Net debt charges also rose steadily until 1935: the volume of debt rose throughout the period, but the fall in interest rates and the increased volume of short-term financing in 1936, allowed the total interest charge to decline slightly in that year. Nevertheless in 1936, net debt charges accounted for 23% of expenditure, as against 19% in 1930, and welfare, the largest single item, accounted for 32% as against 21% in 1930. The services that had been cut to allow these increases were mainly the domain services, the grants to municipalities, highway maintenance, agriculture, and education. Only welfare

debt, and justice (police) received larger expenditures in 1936 as against 1930. The cuts in other services were made mainly to 1932, since when most of them have recovered some of their losses. In the depression, the significant cuts were made in domain (reduced by $1.6 million between 1930 and 1933), highways (reduction of $1.4 million), education ($1.2 million) and municipal grants ($1.1 million). In the recovery years after 1934, highways, education and domain each received increases, but in 1936 none were back to their pre-depression level. In short, the incidence of the depression lay largely on the municipal grants, and public domain, with education suffering also, and some public works being postponed.

On the revenue side, even before the boom broke there were indications that the province would have to reverse its tax reduction policy and in 1929 it was decided that the gasoline tax would have to be raised from 3 to 5 cents per gallon; a new fuel oil tax was also proposed, partly to reduce the margin in cost between coal and fuel oil as motive power, and to enlarge therefore the coal production within the province. In 1931 further changes were necessary to meet the situation imposed by the world depression. In order to distribute the costs of education more equitably, the grants from consolidated revenue were to be increased, and a reduction in taxation of real property was to be made. The Taxation Act was altered, and a tax of 1% was imposed on all classes of income, except on those below $15 per week, and $25 in the case of married persons. At the same time the corporation taxes were increased from 2% to 2¼% of gross income, and the licences on banks were increased by 20%. In 1932 further adjustments had to be made, emergency imposts had to be sought,and a three years' retrenchment policy was announced.A major change was made in the income tax,the gross income tax on trades,professions and businesses,and the income and special revenue taxes,being consolidated into one tax on a graduated scale,new exemptions were made as follows:to single persons

no exemption, to married $500, for dependents $200, for life insurance premium up to $300. The new rates were 1% on taxable income up to $1,000, and increases of 1% up to $19,000: above that income to be taxed at a flat rate of 10%. Corporations and joint-stock companies were subject to those rates without exemptions.

In addition, a new education tax of 5 mills was imposed on lands outside school districts. The fuel oil tax was imposed at one-half cent per gallon, and the gasoline tax raised from 5 to 7 cents per gallon. The amusement tax remained unchanged at 5%, but previous exemptions on admission charges up to 65 cents were removed, and the tax applied to all sports. The tax on pari -mutuel bets was to be raised from 5% to 7%. A tax of 5% was imposed on liquor sales. The municipalities were to take over a share of certain services that lay on the provincial government - mothers' pensions, hospitals, industrial schools and sanatoria.

In 1933 a surtax was added to income tax, 1% on first $2,500 over $5,000, to 18% on incomes over $50,000. An additional lewy on succession duties, in the form of 25% surtax was imposed, and heavier rates imposed on legacies to strangers. The province also discontinued certain grants to municipalities (share of liquor profits and pari-mutuel tax). These changes in municipal revenues coincided with their new expenditure requirements on unemployment, so that they found themselves in financial difficulties, and were unable to meet sinking fund payments. In 1934 a department of municipal affairs was established to study the position, the real property tax being inadequate to meet the municipal needs. In 1936, as the provincial budgetary position improved, some aid was given to the municipalities by the province relieving them of charges imposed on them in 1932.

Despite the tax changes, revenues fell by 22% between 1929 and 1933, the most significant declines being in liquor profits ($2.5 million) and in domain revenues ($1.8 million), the decline in forest revenues being the main contribution to the latter. The yield of taxes and licences also fell during this period, taxes by almost $850,000 and licences by over $575,000. The decline in tax revenues as a whole occurred despite the increase in gasoline taxes ($1 million) income tax on persons ($0.8 million) and fuel oil tax ($0.5 million). These increases were more than offset by the big fall in corporation taxes, that exceeded $2 million, the decline in real property taxes ($0.4 million) and in succession duties ($0.5 million). In the recovery period, the tax revenues reached new levels, the main increase between 1933 and 1936 being in corporation taxes, particularly in taxes on the income of metal mining companies. The total corporation taxes rose by $2.6 million, the gasoline tax by another $0.7 million, the succession duties by $0.5 million, and small increases were recorded in real property, amusement and fuel oil tax. The income tax on persons remained below its 1933 level as a result of rate adjustments. On balance tax revenues have tended to become more important in the total revenue system, having yielded 45% of revenue in 1929, and 52% in 1936. Licences also recovered from the depression, and their total yield in 1936 was above the 1929 level: But domain revenue and revenue from liquor control failed to recover their depression losses, and in 1936 they yielded only 27% of the total revenue as against 37% in the boom days.

In the depression years, the contraction of revenues, and the new expenditures directed attention again towards British Columbia's relationship with the Dominion. On the one side, the expenditure burden of the Pacific Great Eastern Railway loomed large. In 1934 the province contended that the

railway had been built originally as a branch line to the Grand Trunk Pacific, and that "elementary principles of justice and fairness should compel the government (Dominion) to take over the Pacific Great Eastern as part of the national system of Canada". On the other side, the province pushed its claims against the Dominion for increased grants, particularly with respect to retroactive payments for provincial expenditures on the Railway Belt and Peace River Block that had been given to the Dominion at union, and reconveyed in 1930 to the province, and also with respect to the special geographical and fiscal situation of British Columbia in the federation. In 1934, the province was given an additional interim grant of $750,000. Even with this addition, British Columbia was receiving only 5.7% of its revenues from Dominion grants in 1936-7, Ontario alone receiving a smaller share of its net revenue from this source.

With respect to debt history from 1930 to 1936, the significant item has been the cost of unemployment. The depression hit British Columbia severely, and the net value of production fell from 100 in 1929 to 45 in 1932, whereas in the Dominion as a whole, the fall was from 100 to 52. Since then, the recovery in British Columbia has been faster than in the Dominion as a whole, but so also has been the growth of population. The net effect has been a steady rise in direct relief costs from 1932 to 1935 with some decline in 1936, but not enough to get below the 1933 level. The mildness of winter has added to the numbers of unemployed transients in the province. The amount of relief paid in 1936 (Dominion, provincial and municipal) in British Columbia was comparatively high, and on a population basis was exceeded only by Saskatchewan. The outstanding debt now stands at $177.9 million, almost $62 million above the 1929 level.

<u>Summary</u>

(1) Geographical conditions have greatly affected British Columbia's expenditure needs. The mountainous areas, and scattered distribution of part of the population over these areas, affect the costs of government institutions, and transport. Further utilization of this equipment would lower its "overhead" cost, and on the other hand, further widening of frontiers would add to the equipment needs.

(2) The diversity of resources, and absence of serious seasonal disturbances, create a presumption of fairly steady economic development. These favourable factors are partly offset by the position of this province with respect to its markets, and the importance of rail and water freight rates in the prices at which it can offer its commodities in these external markets.

(3) The tax system of British Columbia has since 1917, depended largely on the use of the personal and corporation income tax. The early institution of the income tax in British Columbia was partly associated with the nature of the region, which produced a certain pooling of wealth and population in a comparatively small area of the province. The psychological atmosphere was not averse to this form of taxation, and with improvements of tax machinery, and the need for revenue, this form of taxation continued, and was enlarged as one of the main forms of revenue. The income tax on corporations, mining companies and persons gives over one-third of total taxes; the steady expansion of the gasoline tax has raised its importance, and after the various income taxes it is now the second largest source of tax revenue.

The liquor profits and the domain revenues are still outstanding items in the revenue scheme although they have failed to recover their pre-depression levels.

(4) On the expenditure side, British Columbia makes a

distribution that is closely comparable with that for the provinces as a whole. The net debt charges in 1936 were 23% of total expenditures for British Columbia and 21% for all provinces; the welfare charges were 32% in British Columbia as against 35% in all; in British Columbia 14% goes to education, as against 12% in all provinces. The distribution on highways was the same (8%, and on domain (5%). With respect to its expenditure distribution, British Columbia is, in a statistical sense only, the average province.

(5) With respect to debt growth, the permanent factors affecting it have been factors of settlement and development. The outstanding items of highways, and the Pacific Great Eastern Railway, represent investment for these purposes. Since 1930 the relief problem has injected a third factor into the debt growth, but apart from that, government investment has been directed particularly at the peculiar needs of the region with respect to transport, to institutions (including the university), and to more intensive industrial and settlement aids (e.g. loans to Land Settlement Board, Soldiers' Land Act, Conservation Fund, agricultural credit, etc.). On an accounting basis, the capital losses on investment have been not inconsiderable.

APPENDIX I.

TABLE I.

$ Millions.

	Imports $ (a)	Imports: Percentage change from previous year	Customs Duties: Fiscal Year	Customs Duties: Calendar Year (c)	Customs Duties: Percentage change from previous year
1900	176.5		28.2	28.3	
1901	182.6	+ 3.5	28.3	30.1	+ 6.4
1902	203.4	+ 11.4	31.9	34.2	+ 13.6
1903	251.8	+ 23.8	36.7	38.6	+ 12.9
1904	249.2	- 1.0	40.5	41.0	+ 6.2
1905	263.6	+ 5.8	41.4	43.8	+ 6.8
1906	312.3	+ 18.5	46.1	49.4	+ 12.8
1907	363.0	+ 16.2	39.7(b)	55.8	+ 13.0
1908	282.6	- 22.1	57.2	49.7	- 10.9
1909	339.6	+ 20.2	47.1	56.7	+ 14.1
1910	429.0	+ 26.3	59.8	68.7	+ 21.2
1911	506.3	+ 18.0	71.8	81.6	+ 18.8
1912	626.0	+ 23.6	85.1	105.2	+ 28.9
1913	654.9	+ 4.6	111.8	106.6	+ 1.3

(a) Imports of merchandise (ex. gold) for consumption, compiled for calendar years by Professor F. A. Knox.

(b) Nine months.

(c) Customs duties by fiscal years, Canada Year Book, 1937, p. 826. Recalculated on calendar year basis.

TABLE III.

$ Millions

	Home Investment + Exports $ (a)	Home Investment + Exports Percentage change from previous year	Provincial Revenues (b)	Subsidies from Dominion (c)	Revenues raised by Provinces $	Revenues raised by Provinces Percentage change from previous year
1900	304.3		13.3	4.3	9.0	
1901	332.3	+ 9.2	14.1	4.3	9.8	+ 8.9
1902	369.0	+ 11.0	14.8	4.4	10.4	+ 6.1
1903	411.2	+ 11.4	16.4	4.4	12.0	+ 15.4
1904	405.9	- 1.3	17.8	4.5	13.3	+ 10.8
1905	476.2	+ 17.3	18.8	5.0	13.8	+ 3.8
1906	582.0	+ 22.2	23.8	7.5	16.3	+ 18.1
1907	602.1	+ 3.5	28.0	8.2	19.8	+ 21.5
1908	603.6	+ 0.2	31.7	9.1	22.6	+ 14.1
1909	667.8	+ 10.6	34.5	9.2	25.3	+ 11.9
1910	773.2	+ 15.8	36.4	9.3	27.1	+ 7.1
1911	856.2	+ 10.7	42.8	9.7	33.1	+ 22.1
1912	1,021.4	+ 19.3	50.0	11.7	38.3	+ 15.7
1913	1,117.6	+ 9.4				

(a) A. Cairncross, Die Kapitaleinfuhr in Kanada, Welt Archiv. November 1937, Table 14.

(b) Canada Year Books, Provincial fiscal years recalculated into calendar years.

(c) Fiscal years recalculated into calendar years.

TABLE II.

$ Millions.

	Dominion Ordinary Surplus	Balance of Merchandise Trade	Customs Duties Collected	Duties paid by borrowed imports
	(a)	(b)	(c)	(d)
1900	+ 5.6	- 20.5	28.3	3.3
1901	+ 7.3	- 12.4	30.1	2.0
1902	+ 14.3	- 13.0	34.2	2.2
1903	+ 15.1	- 49.9	38.6	7.6
1904	+ 7.9	- 73.1	41.0	12.0
1905	+ 12.9	- 58.4	43.8	9.7
1906	+ 21.8	- 58.3	49.4	9.2
1907	+ 19.4	- 109.2	55.8	16.8
1908	+ 1.0	- 33.3	49.7	5.9
1909	+ 22.1	- 70.6	56.7	11.8
1910	+ 30.0	- 148.2	68.7	23.7
1911	+ 37.9	- 222.2	81.6	35.8
1912	+ 56.6	- 274.3	105.2	46.1
1913	+ 35.8	- 212.0	106.6	34.5

(a) Dominion Public Accounts. Consolidated Fund Surplus. Fiscal Years nearest the Calendar Years.

(b) From Professor F. A. Knox's Estimates of Canada's Balance of International Payments, 1900-1937.

(c) Table I, Column 4.

(d) Calculated by applying the average rate of duty collected on all imports, to excess of merchandise imports over merchandise exports.